



THE TITLE COMPANY OF NORTH CAROLINA

A MEMBER OF THE OLD REPUBLIC TITLE INSURANCE GROUP

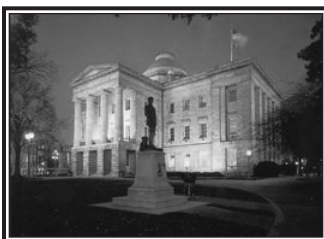
A PUBLICATION OF THE TITLE COMPANY OF NORTH CAROLINA

2010 Legislative Report

The 2010 session of the N.C. General Assembly adjourned on July 10th. Since it was a “short” session, there was not as much before the legislators this term. Much of the focus of the legislature’s attention was dealing with the budget crisis, but a number of bills dealing with real estate related issues were passed. Here are brief summaries of some of them:

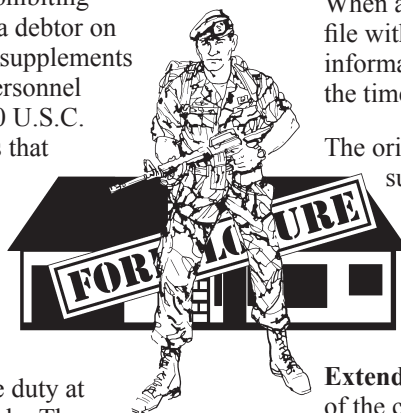
Reconveyance Fees Prohibited—(SB 35)

The problem of reconveyance fees which are charged for the transfer of a lot and which can encumber the marketability of land for long periods of time is addressed in this statute. Transfer fee covenants which require the payment of a fee upon the occurrence of a transfer of real property is now prohibited. Exceptions are made for typical real estate closing costs, governmental fees and charges, reasonable fees to a homeowner’s association, and a fee payable as part of a statutorily authorized conservation or preservation agreement. Effective June 24, 2010, and applies to fees charged after that date (even if the reconveyance document was recorded before June 24th).



No Foreclosure/Soldiers on Active Duty/Funds—(SB1400)

Adds a new section to Chapter 45 prohibiting foreclosure by power of sale against a debtor on active military duty. The new statute supplements the federal protections for military personnel (Servicemembers Civil Relief Act, 50 U.S.C. App. § 501, et seq.) The bill provides that a mortgagee or trustee cannot exercise a power of sale contained in a mortgage or deed of trust, or provided by statute, during or within 90 days of a mortgagor’s or trustor’s period of active military service. It will require a certification by the trustee that the debtor is not on active duty at the time of the hearing before the clerk. There are provisions for waiver by the service member, and the prohibition would not apply to deeds of trust entered into while a member of the armed forces.



Effective January 1, 2011 and applies to foreclosures filed on or after that date.

Judicial foreclosure would still be available to creditors.

Expansion and Extension of State Emergency Foreclosure Program—(SB 1216)

In the face of the ongoing foreclosure crisis, the General Assembly expanded the protection provided by last year’s Emergency Foreclosure program. While that law dealt only with sub-prime loans, the expanded program applies to most residential mortgages (but not equity lines, or construction loans). It requires that notice be given to the debtor at least 45 days prior to the commencement of any foreclosure action; setting forth certain rights and the name and number of HUD approved counseling agencies. The lender must provide the Administrative Office of the Courts (“AOC”) information regarding the notice sent within three business days of mailing to the debtor. The NC Commissioner of Banks will have access to the AOC database of pre-foreclosure filings, and may extend the time for filing the foreclosure to allow efforts by the State Home Foreclosure Prevention Project to avoid foreclosure. Lenders will pay \$75.00 to the Administrative Office of the Courts when they send a pre-foreclosure notice to the debtors to help fund the foreclosure prevention program. The fee can only be charged once per home covered by the Act.

When a foreclosure is actually filed, the Trustee will have to file with the Clerk a certificate that pre-foreclosure notice and information were provided to the debtor and the AOC and that the time periods of the statute have elapsed.

The original Foreclosure Prevention Project, which was supposed to end on October 31, 2010, was extended until May 31, 2013.

Effective July 8, 2010 (as to the extension of the Foreclosure Prevention Project) and November 1, 2010 (as to all residential loans).

Extend Time for Answer to Partition—(SB 1242)

As part of the clarification statute from the 2009 session, this act clarifies that, in a partition action, the Court can grant a thirty day extension to answer (as opposed to the ten day extension available in other special proceedings). Effective July 10, 2010.

Homeowner and Homebuyer Protection Act—(SB 1015)

Places significant restrictions on “Home Foreclosure Rescue Scams”, requiring the payment of at least 50% of the appraised value of a residence, amid other restrictions.

Of more general interest, the law also requires the recordation in the Register of Deeds of any residential lease agreement that is combined with, or is executed concurrently with, an option contract. It also requires recording of any “contract for deed” or “installment land contract”. Buyers are given the right to terminate within three business days of executing the lease agreement, or receipt by the tenant of a signed copy of the lease, whichever occurs last. The lease with option to buy must be recorded within five days of execution.

If the tenant fails to perform, the owner must give at least thirty days notice to cure.

The statute sets out 15 different bits of information that must be included in a residential option lease or a contract for deed. If any of the specified information is left out, it constitutes a violation of Unfair and Deceptive Trade Practices, *per se*.

Once on the record, the only way to remove these clouds on title is to either have the parties mutually acknowledge the termination or to get a judicial order terminating the rights of the tenant. Violation of the statute is made an unfair and deceptive trade practice, *per se* as well.

A seller may not execute an installment sales contract unless it holds title to the property to be sold. If there is an existing deed of trust on the property, a separate written disclosure of the terms of the deed of trust must be given to the proposed purchaser. Effective October 1, 2010.

Orange/Alamance Boundary—(SB 1862) Apparently, there is uncertainty of the boundary line between Alamance and Orange counties, which affects taxation, school attendance, zoning maps, and elections. This statute provides a procedure for establishing a boundary baseline based on a mutually agreed upon resurvey of the Alamance County and Orange County boundary line by the North Carolina Geodetic Survey (NCGS).. Alamance County and Orange County will have to submit a completed survey that includes the N.C.G.S. line and all mutually agreed upon modifications to the General Assembly no later than May 15, 2011

Several other items of particular interest to real estate lawyers were referred to a study committee. Among these items was a Railroad Corridor bill, and reforms to the workmen’s and materialmen’s lien law. Eminent domain issues were again deferred to the next long session.

FORECLOSURE AVOIDANCE:

Part II: Deeds In Lieu Of Foreclosure

In the last edition of this newsletter, we reviewed some of the title insurance concerns which a short sale raises. This month, we continue to look at title insurance issues which could arise with a deed in lieu of foreclosure.

A deed-in-lieu of foreclosure is in many respects similar to a short sale. The biggest difference is that the lender agrees to take the property subject to the mortgage back in exchange for the cancellation of the outstanding deed of trust, or some other consideration. The owner/borrower agrees to convey

the real estate which is encumbered by the deed of trust to the lender. In addition to extinguishing or reducing the amount of the debt, the owner avoids the cost and expense of a foreclosure. The lender is able to avoid both the time and expense of a foreclosure.

There are two problem areas that a certifying attorney needs to be aware of when reviewing a deed-in-lieu of foreclosure. The first is the issue of subsequent liens. A lien which attached after the recording of the deed of trust, (and therefore subject to being cut off by a properly completed foreclosure), will survive and in fact be prior to the recording of a deed-in-lieu. Therefore, a thorough and careful “bring-down” search must be conducted. Any intervening lien should be reported on a preliminary opinion. The title company will require the intervening lien to be paid as a condition of the commitment issued, or will show the exception on Schedule B of the policy.

The second problem is the “equity of redemption” retained by the borrower at the time the deed of trust was given. This is the right the borrower has to pay off the debt in full and take the title back, just as it was prior to the execution of the deed of trust. Courts are very jealous to protect the borrower’s rights and will not allow the lender to “clog” or “fetter” the equity of redemption in any way. Courts recognize that this is a situation ripe for the lender to exercise undue duress against the owner/borrower. To assure that the lender has not taken an unfair advantage, the courts of North Carolina have required that a deed-in-lieu of foreclosure include a statement that the grantor is conveying of his or her own free will, is not insolvent, is not under duress or undue influence and makes the conveyance in consideration of the full satisfaction of the indebtedness.

1 Webster’s Real Estate Law in North Carolina, (5th ed. 1999) §13-20.



Therefore, a successful deed-in-lieu of foreclosure must demonstrate that the deed is the product of an arms length transaction, and is completely the desire of the borrower. Courts will regard the equity of redemption as a precious right, and a subsequent conveyance from the borrower back to the lender will be presumed to be fraudulent. The mortgagee who buys the mortgagor’s equity of redemption has the burden of proving that the transaction was fair and free of undue influence. *Alford v. Moore*, 161 N.C. 382, 77 S.E. 343 (1913).

This proof can be sustained by a showing that the transfer of the mortgagor’s equity of redemption was at the borrower’s initiative, that there was consideration for the transfer, and the mortgagee did not use his power and position to drive an unfair bargain. *Jones v. Williams*, 176 N.C. 245, 96 S.E. 1036 (1918).

Recitals in the deed in lieu and an estoppel affidavit will help to protect the parties from a later claim by the borrower that the deed in lieu transaction was not a free and fair one. Your local office of The Title Company of North Carolina can provide suggested language to include in a deed in lieu of foreclosure and an estoppel affidavit.

If the mortgagor conveys the property by a deed in lieu, but tries to retain certain rights in the lands conveyed, a court may deem the transfer to be less than an absolute conveyance. If the mortgagor retains possession of the property through a lease, or has some other right to re-purchase or re-enter the collateral the courts are likely to deem the deed in lieu of foreclosure as an equitable mortgage. See, e.g. *Beeler v. American Trust Co.*, 24 Cal 2d 1 (1944). If rights under a deed of trust are going to be retained by the borrower, a clear expression of the intent of the parties needs to be made to avoid later controversy.

Another issue which needs to be addressed in considering a deed in lieu of foreclosure is the doctrine of merger. North Carolina courts have recognized the general rule of merger where a smaller interest, such as that of a mortgagee, was “swallowed up” when one person obtained both the mortgage and the full fee simple interest.

Sometimes, a lender may want to retain its mortgagee’s interest separate and apart from the equity of redemption in order to protect against an intervening lien or a possible future bankruptcy. An exception to the general doctrine of merger

exists when the merger would be inimical to the interest of the titleholder. *Washington Furniture Co. v. Potter*, 188 N.C. 145, 124 S.E. 122 (1924) Merger is a flexible principle and is not to be applied mechanically. The facts of each case must be considered so an injustice is not created or the intent of the parties obviously frustrated. *Mosler ex rel. Simon v. Druid Hills Land Co.*, ___ N.C. App. ___, 681 S.E.2d 456 (N.C. App. 2009) A statement of non-merger should be included in the deed of trust to evidence the lender’s intent.

The deed in lieu must be supported by adequate consideration passing between the parties. A deed will not fail for lack of recital of the consideration. *Howard v. Turner*, 125 N.C. 107,

34 S.E. 229 (1899). The lack of a recital of consideration may become an issue if the deed is later attacked as a fraudulent conveyance (which could happen in a bankruptcy context or under North Carolina’s fraudulent conveyance statutes).

Consideration need not be monetary. Consideration sufficient to support a contract or a deed consists of any benefit, right, or interest bestowed upon the promisor, or any forbearance, detriment, or loss undertaken by the promisee. Consideration is the “glue” that binds parties together, and a mere promise, without more, is unenforceable. *Lee v. Paragon Group Contractors*, 78 N.C. App. 334, 337 S.E.2d 132, 134 (1985) disc. rev. denied, 316 N.C. 195, 345 S.E.2d 383 (1986). Therefore, the lender must give up a vested right as consideration for the deed in lieu of foreclosure. In those situations where the lender is not canceling the prior deed of trust, the consideration supporting the deed in lieu should be documented by the closing attorney.

A deed in lieu may subject the borrower to adverse tax consequences. To the extent any portion of the debt is forgiven, the borrower will receive an IRS Form 1099 from the lender. Fannie Mae and Freddie Mac characterize deeds in lieu of foreclosure as “pre-foreclosure sales” and require a two-year time period to elapse between the completion of a deed-in-lieu

and the extension of a new federally insured loan to the borrower.

In the next edition of the newsletter; we will consider title insurance issues which may arise as a result of renegotiations and modifications of existing deeds of trust.

Deed in Lieu Checklist:

- Deed** contains recitals that:
 - Conveyance is absolute and unconditional and freely made
 - Conveyance was for adequate and fair consideration
 - Grantor retains no continuing, contingent or residual rights in the property
 - The deed of conveyance constitutes the only agreement between grantor and grantee (no constructive trusts), or if not, the deed references the settlement agreement or other contingent agreement
- Estoppel Affidavit** signed by all grantors which recites:
 - Conveyance is absolute and unconditional
 - Conveyance was free and voluntary
 - Grantor understood the nature of the conveyance
 - Grantor has given up any and all rights to possession or occupancy of the land
 - Grantor acknowledges that the assurances are for the benefit of the grantee, their successors, heirs and assigns
 - Also recites that the assurances are also for the benefit of the title company insuring the transaction
- Appraisal** or other evidence of value
- Settlement Agreement**
 - Adequate consideration properly documented
 - If forbearance agreement—contains covenant not to sue
 - Unwind provisions, if any, are clearly spelled out

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