

UNIQUE TITLE PROBLEMS THAT OCCUR EVERYDAY

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Real Property Section Annual Meeting
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This manuscript and presentation will focus on the 9 issues which are largest number in sheer volume of title questions (and claims) and the largest source of both claims dollar losses and expenses of that type within the last 4 years.

Title Insurance Claims and related "unique title problems" fall into three large categories:

1. Traditional title claims: Things not revealed by the public record in prior transactions, such as missing heirs and forgeries back in the chain of title.
2. "Quasi-insured-closing" claims: Matters which may involve title issues, but which are created as part of the closing which is the subject of the closing protection letter, such as uncanceled deeds of trust or errors in legal documents (completion, execution, recording, joinder of necessary parties) affecting title to client-owner or proposed insured lender.
3. Insured Closing claims: Matters which are clearly covered *only* by the Closing Protection Letter and would otherwise not be covered by the title insurance policy whether because:
 - the commitment has expired (the ALTA Commitment having a 6-month expiration)
 - the commitment had requirements that were not met (such as failure to obtain an appropriate lien waiver or convert a mobile home to real estate) or
 - the matter does not involve title to real estate (such as failure to deliver the completed closing package to the lender timely or failure to obtain casualty insurance or a septic tank or well report).

Good news: Almost all of these problems are totally preventable!

Bad news: They continue to occur, giving fodder to the fires of those that would seek to change the system for closings in North Carolina (like the FTC) and causing significant losses to clients (whether because the client did not have title insurance or because their personal time and consequential damages are not covered by title insurance).

- Problem #1: Insured Closing Letter: No Big Deal, Right?**
Problem #2: But the lender / realtor told me I didn't need a survey!
Problem #3: "Here's the HUD that proves that old deed of trust was paid. Isn't that enough?"
Problem #4: "Sure I let him use my driveway but I didn't know he was going to put a trailer and a hog barn back there!" AKA "Access – to be or not to be?"
Problem #5: "A Tack by any other name would smell as ? "
Problem #6: "That Darn Contractor!"
Problem #7: The Car Without Wheels and other Mobile Home Nightmares
Problem #8: Clerical error conundrum: When is a "clerical" error no longer a clerical error?
Problem #9: Judgments & Federal Tax Liens: The Good, The Bad and The Ugly (Buyers, Sellers & Bankrupts)
LIST OF EXHIBITS

Problem #1: Insured Closing Letter: No Big Deal, Right?

Over the past decade, losses to title companies from Closing Protection Letters have increased significantly, to the point that most losses can be attributable to errors at the closing table or during the closing process, not from the traditional "hidden losses" for which title insurance was designed. The Closing Protection Letter provides coverages outside of the traditional title insurance policy, including:

- Fraud
- Theft
- Not getting pest or well or septic report
- Not complying with requirements of commitment
- Not assuring all proper parties have duly executed fully and properly completed instruments required by the lender's or purchaser's written closing instructions
- Not recording the documents in the appropriate county registry in a timely manner
- Not submitting property documentation and premium check to obtain final title policy (even if the title company would otherwise have a defense that the commitment had expired or that the attorney did not comply with commitment requirements)
- Not delivering a first lien at closing

The current version used in North Carolina by all major title insurers, pursuant to a filing with the North Carolina Department of Insurance, is explained in the attached Exhibit A, and the actual form of the NCTIRB-01-2003 Closing Protection Letter is attached as Exhibit B.

A major source of expense and loss to title companies (the State Bar and ultimately clients) result from sole or small firm practitioners whose practices are either being discontinued, dissolved or inadequately supervised, recent examples including those in which the attorney:

- Dies suddenly & no financial resource to cover
- Commits suicide
- Just decides to close the door and doesn't take responsibility for their files
- Is too physically ill to continue
- Steals the money, admits it
- Steals the money, disappears
- Doesn't know how to balance and manage their trust account (or closings)
- Doesn't care about balancing and managing their trust account (or closings)

What are some examples of errors in the closing process, whether or not a policy was issued, especially avoidable claims and losses?

- Failure to obtain final policy, send in loan package, get funding number, etc.
- Illegal flipping, where multiple transactions occur at or within a year prior to closing, without adequate financial consideration and without full disclosure to the lender-investor (not just the mortgage broker who is often directly involved in the improper conduct). FHA has recently provided guidance on situations where FHA insurance will be denied on loans in which illegal flips are involved, as set forth in Exhibit C. Many lenders will include requirement in their written closing instructions for inclusion of a chain of title (up to 2 years typically) in either a certification from the attorney or the title insurance commitment *prior to closing*.
- Failure to obtain *written* verification of verbal changes to written closing instructions
- Failure to apply COMMON SENSE! Understand the transaction. The attorney must look behind the "face" of the change to make sure he/she is comfortable with *why* the lender is changing – especially with B-C-D lenders!

OLD ADAGE: "YOU ARE JUDGED BY THE COMPANY YOU KEEP!"

COROLLARY: The FBI, RESPA and others are investigating "bad actors" in the mortgage lending environment and those "clients" are not bound by ethical or moral restraints.

- Regarding Deeds of Trust of the current closing to be insured:
 - Wrong legal description on deed or deed of trust or both
 - No legal description on deed or deed of trust or both
 - Not from all owners or lacking appropriate authority (see below)
 - Refer to "borrower" or "grantor" as all owners, when only some or other parties are borrowers (In re Matter of the Foreclosure of Enderle, 110 N.C.773, 431 S.E.2d 549 (1993)). This is especially a consideration in situations involving spouses where only one spouse is the borrower (below).
 - Inconsistent dates from deed of trust to note (so cannot be foreclosed)
 - Inconsistent amounts
 - Originals not being returned to lenders timely
 - Recorded in wrong county
 - Failure of equity line deed of trust to comply with the provisions of N.C.Gen.Stat. Section 45-81 *et seq*
 - Failure of future advance deed of trust (especially construction deeds of trust prepared out of state) to comply with the provisions of N.C.Gen.Stat. Sections 45-67 *et seq*.

- Regarding closings involving Open Estates, the closing attorney should assess the risks involved in not joining any potential party to the estate. The investigation of both the public records and among the family members and estate fiduciaries and attorneys should include analysis of power of sale in the will, the purpose of the proposed sale or refinancing, the joinder of all devisees and possibly disinherited heirs (if a caveat proceeding is a high risk), creditors of the estate if they are not being paid in full at or before closing, applicable inheritance or estate taxes (depending on the date of death). (See attached Exhibit D for a sample Open Estate Affidavit and Indemnity.) The authority of an executor who is not the devisee of the property, even one granted power of sale in a will, is still an open legal question. Pending potential legislation to address the situation is still being discussed and argued among estate planners, real estate practitioners, title companies and the North Carolina Administrative Office of the Courts.

- Regarding conveyance or subordination to deed of trust of spouse's rights, common issues not addressed adequately include:
 - Joinder of co-owning spouse in executing deed of trust in situations where only one spouse is the borrower, without clearly indicating that the "borrower" is only one spouse and the other is joining sole to release or subordinate their interest in the property
 - Joinder of non-owning spouse to release or subordinate marital interests in conveyances or instruments
 - NOTE: A DEED FROM ONE SPOUSE TO ANOTHER SIMPLY CONVEYING THE FEE IS NOT ENOUGH to waive contingent statutory marital rights, absent sufficient waiver of rights language and compliance with N.C.Gen.Stat. Section 52-10, Section 52-10.1 or other appropriate statutory provision.
 - Equitable Distribution order that orders conveyance but does not follow up with *actual* conveyance by quitclaim or order pursuant to Rule 70 of the North Carolina Rules of Civil Procedure.
 - Conveyance after divorce and severance of tenancy by the entirety, in the face of individual judgments or tax liens against the conveying spouse.

- Erroneously assuming that a voluntary partition deed creates a tenancy-by-the-entireties, contrary to N.C.Gen.Stat. 39-13.5.
- Regarding conveyance pursuant to powers of attorney (*See* Chapter 32A of the North Carolina General Statutes and annotations therein), common issues involve:
 - Gifts only if authorized by power of attorney and a history of such charitable gifts (violation of fiduciary duty to look after assets of the principal)
 - Gifts to Attorney-in-fact only if specifically authorized by power of attorney (old common law self-dealing)
 - Limited power of attorney not authorizing the particular action
 - Using the property for the personal benefit of the attorney-in-fact, not the principal (such as to secure a note from the attorney-in-fact only)
 - Failure to record original power of attorney in county in which property is located for clarity of marketability of title and for reliance in the event of a later revocation by the principal
 - Improper notary acknowledgment of documents executed by the attorney-in-fact
- Regarding property interests owned by minors or incompetents, conveyance or mortgage must be approved either through the proceedings of N.C.Gen.Stat. Sections 35A-1301 *et seq.* or other special proceeding (such as a partition proceeding) typically including appointment of a guardian ad litem, approval by the court and allocation of proceeds to the minor's or the incompetent's interest. Case law is very restrictive regarding the fiduciary purpose of the proposed transaction and the long term effect. In the case of a minor, the parents have legal support obligations and courts have been hesitant to approve sale of their interest in real estate, permanently divesting them of their interest. Even the duration of a typical deed of trust will far exceed the term of the guardianship of a minor. So proof of legitimate beneficial purpose for the real estate transaction can be very problematic. Some successful examples have included situations where the refinance was solely to reduce the interest rate on an already-existing legitimate lien on the property (previously approved by the court or attached to the property prior to the minor obtaining their interest), for major medical needs of the minor or because the property was becoming a significant burden on the minor's estate (needing major repairs or investment to maintain).
- Regarding improperly performed or completed foreclosures, or failure of the record to reveal compliance, due to:
 - Lack of verification of posting, publication, notice to subordinate lien holders, timely certified notice to IRS and application for release of 120-day right of redemption
 - Failure to assure quality of title and resolve title claims prior to attempted completion of foreclosure, especially in situations involving missing parties, erroneous legal descriptions or mobile home titles (more below)
 - Attempted rescission of erroneous foreclosure, resulting in significant clouds on title due to:
 - Lack of authority of the Clerk to rescind a delivered and recorded deed
 - Quitclaim back to borrower, free of encumbrance of the already foreclosed deed of trust
- Regarding taxes and assessments, questions and claims continue to arise due to errors such as:
 - Payable in installments
 - Deferred taxes still due
 - Missed a newly incorporated town and its taxes and assessments
 - Taxes in bankruptcy, deferred but not waived
 - Tax foreclosure missed in title search
- Incomplete chains of title due to:

- Rerecording deed and not deed of trust, so deed of trust is outside of the chain of title pursuant to N.C.Gen.Stat. Section 47-20.
- Names are inconsistent or wrong on documents, so that indexing cannot indicate completed chain of title
- Deeds of trust are recorded in wrong order, establishing an erroneous priority pursuant to N.C.Gen.Stat. Section 47-20, so curative actions (quitclaims or subordinations) are critical
- Deeds of trust recorded simultaneously: If 1st and 2d mortgage are recorded simultaneously, prior to October 1, 2003, they were deemed by law to have *equal priority* or *coparity* absent specific language in the “2d” subordinating to the “1st”. Pursuant to statutory revisions to N.C.Gen.Stat. Sections 47-18 and 47-20, effective October 1, 2003, priority is now determined based, in order of governance, on:
 - (1) terms of document itself (i.e. if it indicates subordination to a later recorded instrument that would control)
 - (2) time of recording,
 - (3) document control number assigned by Register of Deeds and
 - (4) book and page of recording.

Problem #2: But the lender / realtor told me I didn't need a survey!

An increasing source of claims to (and denials) by title insurance companies involve problems which could have been identified by a current accurate survey of a property obtained by and for the particular owner/insured. The often-cited "Survey Coverage Without A Survey" applies to *loan policies only* (other than the limited survey coverage of an "enhanced" or "expanded coverage" policy, the ALTA Homeowners Policy of Title Insurance (1998)).

A corollary problem is that, since no survey is obtained, descriptions are increasingly no longer checked for closure, consistency with address, reasonableness under the circumstances, nor can the location of improvements critical to all parties be identified. Some classic legal description examples:

- Wrong property:
 - Wrong road
 - Wrong unit on platted development or condominium
 - Wrong plat (and therefore the wrong "dirt"), especially a purported condominium referencing only a boundary plat
 - Wrong county altogether
- Improvements are on a different tract of land, though the insured has good title to the tract described as well
- Missing or erroneous calls; description does not close
- Not include all the property, especially where a tract was obtained in multiple deeds
- Including too much property (i.e. entire subdivision tract rather than just the particular lot being sold)
- Legal description simply not attached to recorded documents
- Poorly drawn descriptions, referencing just irons or stumps rather than permanent monuments and adjoining's property lines and calls
- Multiple plats, with changed the property lines or inconsistent easements, setbacks, fill areas or other exceptions
- Wrong county – or relocation of county line

Advising a client not to obtain a survey, or failing to advise the client that a survey is critical to *their* protection, or failing to discuss the ramifications of matters shown on a survey when obtained, is bad advice!! For example:

- Owner not covered because no survey at closing (See attached Exhibit E, " Owners Need Surveys – Still! (Or, The *Risks To You and Your Client* of Lender's "Survey Coverage Without a Survey")
- Fence cuts off part of property – neighbor's cow pasture – adverse possession claim
- Exceptions exclude coverage of matters that would be revealed by a survey about which the client may have a significant interest – creeks, road or railroad right-of-way, or lack of access altogether
- Encroachments into utility rights-of-way or onto or from adjoining's improvements – no owner's coverage
- Survey obtained after closing showing encroachments – post-policy, denied
- Improvements not on insured property
- Boundary line disputes – battle of the surveyors (and we insured both tracts)
- Failure to review survey as compared to title search matters, including plats, restrictions, easements (appurtenant and exceptions)

Problem #3: "Here's the HUD that proves that old deed of trust was paid. Isn't that enough?"

1. *Was it an equity line?*

Especially regarding equity lines, G.S. 45-81(c) provides:

“At any time when the balance of all outstanding sums secured by [an equity line] mortgage or deed of trust pursuant to the provisions of this Article is zero, the lender shall, upon the request of the borrower, [emphasis added] make written entry upon the security instrument showing payment and satisfaction of the instrument; provided, however, that such security instrument shall remain in full force and effect for the term set forth therein absent the borrower's request for such written entry. No prepayment penalty may be charged with respect to an equity line of credit loan.”

If the borrower does not sign the termination or “freeze” request, or if the borrower later changes their mind and the account has not been terminated and the lien canceled, or if the “freeze” request was not in the form preferred by the lender, the bank may and often does prefer to maintain its relationship with the borrower and advance more funds.

2. *Was it really paid in full or was it a short payoff or was it applied to the proper account at all?*

Lenders often refuse short payoffs to avoid a defense of “accord and satisfaction” for having accepted it. They typically do not read payoff cover letters at all. If the borrower has multiple accounts, they may have to “choose” which account to credit or they may have been given the incorrect account by the attorney or borrower in any event.

3. *But the girl at the bank said they would release my client's lot from that big development loan!*

Any agreement to release a particular property should be obtained in writing, prior to closing, including any release fee or other consideration or conditions to obtain the release. A verbal purported agreement to release for no consideration is (a) difficult to prove (your word against theirs) and (b) probably unenforceable under the Statute of Frauds especially if no consideration or release fee paid. And memories change dramatically when the debtor on the prior uncanceled or unreleased loan goes into default and foreclosure! So follow up post-closing should be *immediate and persistent!* (Ditto for Subordinations to protect your lender-clients!)

4. *What is "insured over" anyway? Can you spell "marketability?"*

Your client will learn a hard lesson about marketability of title when they try to sell the property and it has a stack of uncanceled liens! And the longer you wait, the harder it is to find the lender and obtain the appropriate cancellation documents. For example, for a \$100,000 home purchase:

- How many "insured over" prior deeds of trust are too many? Two \$50,000 loans? Four loans totaling \$250,000? Or a prior development loan of \$5 million for which there is no release?
- Who was actually protected by the prior lien being "insured over" – a lender that is now being paid off (and may have simply been insured for priority, not whether the lien still affected the property) or an actual owner with recourse to an ongoing owner's policy?
- Are you really advising your client to put their equity at risk in a situation where their equity is not protected by the policy, such as a construction loan policy situation or a situation where their equity will build up over time?

NOTE: The National Conference of Commissioners on Uniform State Laws (“NCCUSL”) is currently drafting a proposed “Uniform Mortgage Satisfaction Act” for presentation at its August conference. If approved, the Commissioners are hoping to have it presented and adopted in as many states as possible. Members of the Real Property Section Council, the North Carolina Land Title Association, the North Carolina Bankers Association, the North Carolina Association of Registers of Deeds and other attorneys who have expressed an interest have provided comments. The latest draft is available on-line at: www.nccusl.org, under “Select A Committee” choose “Mortgage Satisfaction” and click “Search.” Then choose the May 2004 Meeting Draft for the latest draft (48+/- pages, including all Official Comments).

5. *What are the major sources of claims involving prior deeds of trust?*

- Failure to cancel loans paid at closing (99 FEO 5) – marketability problems
- Not getting payoff or release terms in writing
- Not following requirements for payoff or release (especially internal lender requirements on equity lines)
- Not obtaining updated payoff amounts when closing delayed (especially if loan in default or loan involves an FHA payoff after the end of the month)
- When lender does an internal transfer of funds for payoff, failure to follow up on the post-closing cancellation (REMINDER: The borrower is also your client!)
- Failure to obtain and record adequate subordinations
- Short payoff
- Failure to send payoff letter with instructions to apply and contact immediately regarding shortage
- Failure to follow up on cancellations – short, equity lines, subordinations, releases, full cancellation payoffs
- Failure to “freeze”, terminate and obtain record cancellation of equity line deed of trust
- Subordination or payoff of *wrong* deed of trust

Problem #4: “Sure I let him use my driveway but I didn’t know he was going to put a trailer and a hog barn back there!” AKA “Access – to be or not to be?”

1. *You didn’t tell me that road shown on that map is a private road!*
 - *I’ve been getting billed \$300 quarterly for maintenance. Who pays for that?*
 - *I just got a \$17,000 assessment bill for road improvements!! I can’t afford to pay for that and will lose my house!*
 - *The road washed out and no one else wants to contribute to fix it!*
2. *Sure there’s a driveway, but it’s not on that easement.*
3. *Sure there’s a driveway easement, about 8’ wide at most. That’s it!*
4. *Sure there’s a driveway. This is a family farm and it leads to all of our houses. And we told that mean old banker not to foreclose on our brother!*
5. *That easement only gets you across Joe’s land to Sam’s land. The public road is still a mile (or 5 feet) away!*

The closing attorney should be very clear on the *legal* access to the property, the title, the creating document, maintenance responsibilities, adequacy for the client’s needs and client’s knowledge of the situation. Consult legal treatises or CLE manuscripts on the subject (of which there are many excellent ones) if it is unclear, or contact the title insurer. (This topic is far too broad and complex to cover in this presentation.) *The client should be advised from the title search if their access is private or public road and, if private, of the ramifications to them.* If restrictions or a maintenance agreement provides for assessments, or if the road is private, the client needs to know how and by whom the access roadway will be maintained. Often lenders require similar assurances as this is a fundamental FHA, VA, FNMA, FHLMC requirement. The access means probably should have been disclosed to the lender in the appraisal, though the closing attorney would presumably rarely know about that.

NOTE: ALTA title insurance policies (other than the 1998 Homeowners “expanded coverage” or “enhanced” type of policy) typically only insure access in general, not access to reach a specific public road and not title to a specific private access easement *unless* the attorney has certified title to that particular private access right and the specific access right has been included as insured land under Schedule A of the policy.

6. *What are the major sources of claims involving access?*
 - Overburdened easements because our tract was subdivision of the original benefited tract
 - Property which the easement crosses is being condemned or foreclosed or sold to satisfy judgment
 - Agreement does not include utility rights
 - Not clearly defined or located/locatable
 - Not sufficient (width or maintenance) for intended purpose
 - Does not reach all the way to the insured fee property or to a public road
 - Shared with others and crosses our property, preventing the improvements location planned

Problem #5: “A Tack by any other name would smell as ?”

RPC 99 (attached as Exhibit F) provides that tacking is within the ethics requirements governing NC attorneys’ real estate practices, subject to certain limitations such as tacking only to owner’s policies and with full disclosure to the clients. It has become a very common in many areas, due to economic realities.

Title insurance companies may *insure* properties even if the attorney’s tack has not strictly complied with the ethical rules, i.e. tacking to loan policies on occasion. This is a matter of contract between the attorney and the title company, and a risk analysis on behalf of the title company.

However, tacking is highly risky and should be undertaken cautiously and carefully by the attorney. The prior title policy should be examined carefully, including review of record documents noted in the policy, comparison with your client’s survey (if one is obtained) or plans (if construction is proposed) and a “common sense” review. The attorney should consider if they trust the quality of the prior closing attorney’s work, if the policy itself contains appropriate detailed exceptions versus generic ones, what the risk to the client will be if the prior policy does have an error (for example, new construction contemplated versus existing improvements), and how risky the neighborhood or the development itself may be. If even considering tacking to a *loan* policy, the attorney should contact the prior title insurer and make a determination (a) why an owner’s policy was not issued and (b) what significant title defects were “covered” for a lender that would be inappropriate for an owner. A few significant and costly examples:

1. *Oops. Wrong property.*
2. *Oops. The prior policy only included Tract A, not Tract B or the easement for access.*
3. *But the prior policy said that my lot was on that plat!*
4. *What do you mean they can’t build what and where they plan to build? But that easement wasn’t in the prior policy! My client should have known I was tacking and that there might be easements not mentioned in the prior policy that prevented them building their proposed commercial enterprise without my having to disclose to them.* Commercial properties being developed and easements missed in prior policy, causing major negotiation with benefited easement holder, reconfiguration of commercial development and/or significant additional development costs.
5. *I tacked to a loan policy. How was I supposed to know it was only lender’s coverage for a small loan and everyone knew the borrower didn’t really have full fee title at all?*
6. *What are all these generic exceptions?* Some policies are being issued with "generic" exceptions for restrictions, easements and other matters, indicating that the prior attorney did not do a full search or tacked to a policy which was not based on a full search. A specific example would be the "Short Form Loan Policy" which, by design for the easier review by lenders, does not reflect specific exceptions critical to a purchaser.
7. *What does the Preliminary Opinion on Title (NC Bar Assoc. Form No. 1-P 1989) mean that, in tacking, the attorney certification includes:*
“[H]as a search of the public records been accomplished for such period of time within which judgments, liens or other matters could affect the property, regarding the owner(s) of the property on and after the date of said policy?”
If prior searchers did not address their "buyer" judgments and liens, for example in a purchase transaction, these liens will not appear in the title policy. A subsequent searcher places their later client (new purchaser or lender) at serious risk if they have not identified and addressed these matters as a part of their search. And the prior policy will not be clear on this.
8. *But if the title company will "insure over" what's the problem?* “Insuring over” is not automatic and, in many cases, not even sufficient to be desirable. For example, the following are just a few key times when it is probably *totally inappropriate*, for protection of your client, to assume or

even request continued coverage. Instead the attorney should strongly advise remediative action immediately, possibly even the filing of a title claim by the already insured owner:

- (a) Requesting an increase the policy coverage, when it may not have been enough to cover the potential loss to begin with – especially when coupled with b below . . .
- (b) The prior coverage is a lender policy only. (That policy and coverage disappears as soon as the loan is paid off, whether by refinance or sale.)
- (c) The outstanding issue is one that won't expire or go away with time, such as:
 - i. A missing signatory (such as a spouse or missing heir).
 - ii. A minor or an incompetent.
 - iii. A prior outstanding (missed or uncanceled equity line) deed of trust or recent judgment.
- (d) The outstanding issue is for a judgment, deed of trust or other lien (or combination of liens) that are *not* paid and exceed the outstanding coverage.
- (e) Improvements violate restrictions (such as against mobile homes or setbacks), especially if they were post-policy (if the prior loan was for construction, especially) or known by the owner but not disclosed to us or covered in their prior *owner's* policy.
- (f) Mechanics' liens for construction contracts entered into by the *current owner* or *post policy*.
- (g) Mobile home titles not having been canceled.
- (h) The outstanding issue is for an outstanding unpaid judgment or deed of trust that was the obligation of the *current owner*. (This may have been insured over because the earlier deed of trust was a purchase money or because a payoff was submitted but was short and *this owner* refused to make up the shortage.)

9. What are the major sources of claims involving tacking and title searching?

Title Insurance: (RPC 99)

- “Updating” from policy on different property
- Inadequate search period
- Tacking to loan policy rather than owner's policy
- Tacking without notice and permission of client
- Not obtaining owner's coverage
- Not obtaining enough owner's coverage (especially in commercial situation)
- Not adequately reviewing prior policy and its exceptions
- Not fulfilling requirement for necessary endorsements
- Not clearing problems with title company *prior to* closing

Title Search:

- Not checking all documents in chain of title
- Missed deeds of trust, judgments, easements or other exceptions
- Not updating when record (Clerk's office and Register of Deeds)
- No conveyance of common areas to association
- Not checking temporary indexes
- Not fully reviewing estate and foreclosure files
- Not checking judgments on all owners, especially beneficiaries of estate

Problem #6: “That Darn Contractor!”

1. *But I got a “lien waiver” from the seller at the closing and he also signed as the contractor.*

A common source of significant claims is the misperception that a purported “lien waiver” by the seller-builder or seller-developer actually waives any liens under Chapter 44A, Article 2, of the North Carolina General Statutes. In fact, N.C.G.S. § 44A-8. Mechanics', laborers' and materialmen's lien; persons entitled to lien, provides:

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 of real property for the making of an improvement thereon shall, upon complying with the provisions of this Article, have a lien on such 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 such contract.

The statute specifically does not require that the “person” be a licensed contractor, and specifically does not allow the owner to effectively “waive” the liens of those with whom they contract, even if the “owner” also happens to be a licensed contractor and the “persons” might be otherwise considered subcontractors for licensing or general industry descriptive purposes. Title insurance companies routinely work with certain developers and builders and do make risk determinations whether to rely on what are really unsecured indemnities from them. However, these should be specifically discussed with the title insurance company *prior to closing* as it is strictly a matter of discretion of the company. The typical title insurance commitment will have a Requirements in Schedule B, Section 1, that sufficient waivers or indemnities be provided regarding any potential mechanics’ or materialmen’s liens for work or material provided within 120 days prior to closing. If this requirement is not met (i.e. an insufficient “lien waiver” is provided), the title company may choose not to cover these matters if not already agreed to prior to closing.

In the event any construction is contemplated immediately following closing, and especially if any portion of it is already in process, adequate subordinations must be obtained *from all persons who have contracted directly with the owner* and are, therefore, entitled to liens under N.C.G.S. 44A-8, including surveyors, appraisers, contractors (or even purported “subcontractors” if they have contracted directly with owners), rental companies, suppliers. Each lien of the particular “person” will relate back to the beginning of construction if it is an ongoing contract. In situations where a true independent general contractor controls the construction and has contracted with the owner, this may be a simple process. If the owner is also planning to serve as their own general contractor, the situation should be discussed with the title insurance company *prior to closing* to assure what subordinations or indemnities may be necessary.

2. *And the seller/builder is a big developer, very well know. I didn't think those liens were a problem since they weren't on my property.*

Any notice of any lien filed against a builder may be a red flag indicating further problems are forthcoming. All transactions and all entities should be considered within the light of current circumstances of the parties and the economy, even and possibly especially those with long-established builders. In one example alone, in Kentucky and Ohio, a single long-time well-respected builder of upscale homes, Erpenbeck Construction, was responsible for a scandal in which several members of the Erpenbeck family are facing federal and state prosecution and potential prison time and a bank with which they transacted business has failed. Most funds were lost because the closing attorneys (on a few)

and settlement services (on most) gave the payoff and release checks, payable to the bank, to Erpenbeck employees to deliver! These employees delivered them, but many were delivered to the Erpenbeck account itself or applied for other purposes than the intended releases. Many of the homebuyers did not have owner's title insurance coverage due to the additional cost (not simultaneous issue) and were thus out of pocket for substantial losses. According to The Cincinnati Post, 2-7-2004, the Erpenbeck scandal "by the numbers" involved:

- **\$33 million:** Amount of homebuyers' payments misdirected into Erpenbeck Co. accounts over the course of three years. About \$26.28 million worth of those checks were not repaid at the start of the investigation. As part of his plea deal, Bill Erpenbeck has agreed to pay back what's left of the debt.
- **260:** Homeowners defrauded
- **200-plus:** New homes with liens placed on them due to millions of dollars in unpaid bills to subcontractors. Attorneys representing homeowners later got all the liens removed through a negotiated settlement.
- **295:** Transactions in which 10 federally insured construction lenders were defrauded by Erpenbeck.
- **3:** People who have pleaded guilty to bank fraud so far in the ongoing FBI investigation: Bill Erpenbeck, who admitted he led the scheme; his sister, Lori Erpenbeck, who admitted her role in perpetrating the scheme as the head of the company's accounting, and Michelle Marksberry, the company's closing agent, who admitted she participated in stealing checks that were supposed to be paid to Erpenbeck's lenders but were instead deposited into Erpenbeck accounts at Peoples Bank of Northern Kentucky and Firststar Bank, now U.S. Bank.
- **2:** Individuals still under investigation: Former Peoples President John Finnan, who in one taped April 2002 conversation with Erpenbeck discusses how Finnan kept a loan to cover a \$4 million overdraft secret from the bank's board, and then-Executive Vice President Marc Menne.
- **\$10 million-\$12 million:** Amount that some 200 Peoples shareholders argue they lost through the plummeting value of their bank shares.
- **10** Number of months since Bill Erpenbeck pleaded guilty to one count of bank fraud for leading the scheme.

3. *Well, they said they weren't going to start construction until after closing, so we didn't bother with getting a contractor's subordination. But the closing got delayed.*

Even, possibly especially, in purchase-construction situations, care must be taken to obtain subordinations from all person who have dealt with the purchaser as well. *See, for example, Dalton Moran Shook, Inc. v. Pitt Dev. Co.*, 113 N.C. App. 707, 440 S.E.2d 585 (1994), and *Carolina Builders Corp. v. Howard-Veasey Homes, Inc.*, 72 N.C. App. 224, 324 S.E.2d 626, *aff'd* 313 N.C. 597; 330 S.E.2d 606 (1985).

4. *"X Building Supply Company" signed a release deed. Doesn't that release their materialmen's liens as well?*

Also note that a deed of trust by a building supplier is a separate lien from the mechanics' lien. Separate releases and waivers should be obtained for each.

In troubled times when builders and developers have been too aggressive in developing and have properties they are unable to sell in a timely fashion, these are a significant source of losses for owners, lenders and title insurance companies.

Problem #7: The Car Without Wheels and other Mobile Home Nightmares

1. *It's listed with the tax department and they say it has a "skirt." Isn't that enough?*
2. *But the house has been there for years!!*
3. *But the lender says they need an ALTA 7!*

The new statutory provisions allow a "clean" way to assure that a mobile home has been converted from personal property under the Uniform Commercial Code (Chapter 25 of the North Carolina General Statutes) and the Motor Vehicles statutes (Chapter 20 of the North Carolina General Statutes) to real estate governed under Chapters 44A, 45, 47 and other real estate related provisions of the statutes. More detailed information, statutes, forms, procedures (bonding and user code access) and flowchart are available on the Chicago Title Insurance Company, North Carolina web site at the Bulls, Bulletins & Articles page (www.northcarolina.ctt.com/docs/word/MOBILEHOMES5-4-02)

PreConditions which should be completed *prior to* instituting (and especially completing) sale, refinance or foreclosure on the land:

1. Home must be on permanent foundation with wheels, tongue, axle removed, and must be listed as real estate for tax purposes, under G.S. 105-273(13), or to be so listed at the next tax listing period.
2. Information must be gathered identifying the home and potential owners in whose names the home might be listed. Serial numbers, manufacturer, model and model year for each section home must be obtained, usually by appraiser. For example, a doublewide may have 2 or more serial numbers, one for each section, or may have a single number with designations of "A & B" for the sections. In addition, the names of owners of the "property" since the home was purchased (typically since its model year) should be obtained from the public registry (to do complete DMV search below). Any Manufactured Housing Riders, conveyances with the home included as part of the legal description or other forms or information indicating the intent of the borrower that the home be included as real estate should be gathered as potential exhibits or evidence for the foreclosing counsel to determine the appropriate procedure below.
3. DMV search is required, preferably in writing, to determine if a Certificate of Title has been issued under (1) serial numbers and (2) name(s) of potential owners since the home was placed on the lot. Confirmation should be obtained *in writing* so 3-4 week lead time will be required to obtain reliable written verification. DMV can be contacted as follows:

Division of Motor Vehicles
Vehicle Registration Section
Mail and Distribution Unit
3148 Mail Service Center
Raleigh NC 27699
1100 New Bern Avenue
Raleigh NC 27697
Phone: 919-861-3639
FAX: 919-733-6941

For those dealing with mobile or manufactured homes regularly, DMV offers a special telephone service, as a "telephone subscriber," using a user code, for a fee billed monthly of \$1.00 per call. A

similar service may also be available by e-mail. Otherwise, the Federal Driver's Privacy Protection Act of 1994 prohibits the DMV from disclosing personal information, which includes photographs, social security number, driver license numbers, names, addresses, telephone numbers and medical or disability information among other things. The attorney should request the user identification code by contacting either Carol Howard, Director, or Diane Johnson, Assistant Director, of the Vehicle Registration Section, at (919) 861-3332. Thereafter, the attorney could use the user code for a telephone request or submit [DMV Form MVR-605A](#) via facsimile for each request. Forms and information are available from DMV on their web site at: <http://www.dmv.dot.state.nc.us/VehicleRegistration/forms/>

6. *What are the major sources of claims involving mobile homes?*

If the DMV Certificate of Title is still outstanding, the home remains *personal property* pursuant to the Uniform Commercial Code (Chapter 25 of the North Carolina General Statutes) and the Department of Transportation statutes (Chapter 20 of the North Carolina General Statutes) until filing and recording of the Form MVR-46G pursuant to G.S. 47-20.6. Conversion / cancellation procedure must be completed. DMV Form MVR-46G Affidavit for Removal of Manufactured Home from Vehicle Registration Files pursuant to G.S. 20-109.2 and G.S. 47-20.6 must be executed and filed with the DMV and, once signed and returned by DMV, with the Register of Deeds. This will also require release by any record lienholders as well as execution by the "owner" of both the home and the land.

If the Certificate of Title of the home is in the name of the current owner of the land, curative possibilities include:

1. Having the landowner sign and file the MVR-46G Affidavit.
2. Having the landowner/home title holder transfer the title to the Lender (in a deed in lieu of foreclosure situation) and Lender complete MVR-46G procedure once foreclosure is complete.
3. If the Lender is the named lienholder on the Certificate of Title, an action for claim and delivery should be instituted *before completion of the foreclosure* (more on this later), followed by MVR-46G procedure by Lender once foreclosure is complete or Substitute Trustee as part of foreclosure process.
4. If the lender still named on the Certificate of Title as lienholder is from a prior loan and is not the Lender, but was, for example, a lender paid through the Lender's closing or for which closings and payoffs can be traced, Lender could seek assignment of that lien and institute an action for claim and delivery on the home *before completion of the foreclosure* (again more on this later), then complete MVR-46G procedure.
5. Civil Action seeking Order to DMV to transfer Certificate of Title up to and including complete judicial foreclosure.

If the DMV Certificate of Title of the home is in the name of a prior owner, curative possibilities include:

1. Locating that prior owner and have them execute a transfer of title to the home to the Lender. (They *cannot* file an MVR-46G because they are not the owner of the property.)
2. Bonding procedure under G.S. 20-76(b) through the DMV may be considered to transfer the title to the current record owner of the land, if sufficient evidence from the intervening conveyances and documentation can be obtained to satisfy DMV and the bonding company; then current owner must complete MVR-46G procedure.
3. Civil Action seeking Order to DMV to transfer Certificate of Title up to and including complete judicial foreclosure.

If NO DMV Certificate of Title is outstanding (whether because never issued or because "canceled" pre-1/1/02), a Declaration of Intent should be filed pursuant to G.S. 47-20.7 by the "owner" of both the home and the land. Some possibilities include:

1. Declaration of Intent signed by the owner of the land who is purportedly also owner of the home.
2. Trustee's foreclosure deed incorporating a fully completed and executed attached Declaration of Intent, based on the Manufactured Home Rider in the deed of trust, or because the home was included as part of the legal description conveyed in the original recorded deed of trust, thus rendering the trustee the "owner" pursuant to the Deed of Trust conveyance.
3. Declaration of Intent signed by the purchaser of the land at the foreclosure, based on the original deed of trust and foreclosure proceeding including the home as part of the legal description.

Title Insurance issues with regard to insuring mobile home as real estate, either from prior policy or current proposed coverage:

1. Completion of the statutory requirements of filing a Declaration of Intent is a post-policy, regulatory matter that must be handled as part of the closing or foreclosure. It is not a covered risk but a requirement of subsequent closing, much as the new closing or foreclosure is not a covered matter under the old policy, but is a new requirement for new coverage at the new transaction.
2. If a Certificate of Title remains outstanding, the home is personal property. "Land" insured under a title insurance policy does not include personal property, unless an ALTA 7 was also issued with the policy.
3. If an ALTA 7 was issued with the prior policy, attorney / lender due diligence should include an adequate DMV search of the status of the DMV title *pre-closing / pre-foreclosure* and filing a claim under a prior policy should be done *immediately* if a Certificate of Title is outstanding. Curative possibilities should be discussed with the title insurer prior to proceeding with the closing or foreclosure.
4. UNDER NO CIRCUMSTANCES SHOULD A MORTGAGE LENDER OR FORECLOSURE COUNSEL OBTAIN A RELEASE OF THE PRIOR LIEN ON THE DMV TITLE, ESPECIALLY IN THE FORECLOSURE CONTEXT, AS THIS VESTS THE TITLE IN THE OWNER FREE & CLEAR OF LIEN. This may seriously impair the ability of the title company to respond to the claim and thereby justify a denial of any coverage under the policy.
5. In the foreclosure context, the above should be completed *prior to foreclosure* and after consultation with the title insurer . If a Lender completes the foreclosure prior to filing the claim on their existing loan policy, even with ALTA 7 endorsement, the coverage may have been forfeit either because:
 - No deficiency remains on which to seek claim and delivery. Lender suffers no loss since they obtained full value through the foreclosure bid, and/or
 - Completion of the foreclosure may prejudice the ability of the title insurer to render the title as insured by failing to provide timely notice of claim (prior to foreclosure when remedies were more easily obtainable). Any civil action may have to include not only a request for the title transfer, but also *to set aside the foreclosure done by the requesting lender*, a matter which may stress the court's tolerance and lead to very uncertain results!

Some Possible Civil / Curative Actions include:

- Reformation action to obtain Court Order that the deed of trust included the home as real property
- Court Order to DMV to transfer or cancel the Certificate of Title
- If post-foreclosure, the action may need to seek rescission of the foreclosure action itself and institution of either judicial foreclosure or at least authorizing a new foreclosure proceeding once title to the manufactured home is determined.
- "Quiet Title" type of action to quiet title to the home in the lender
- Claim and Delivery on the home by Lender/

Problem #8: Clerical error conundrum: When is a “clerical” error no longer a clerical error?

1. *If it’s just clerical, why do we need to re-record? What is “clerical” anyway?*

According to Ballentine’s Law Dictionary (Lexis Law Publishing, 1969, updated through 1998), a “clerical error” is defined as:

“An error in technique rather than in substance of thought; the misprision of a clerk or other officer of the court, causing a defect or omission in the record. As the phrase applies to the record of a judgment, it means the failure to preserve or correctly represent in the record, in all respects, the actual decision of the court. Annos: [10 ALR 589](#), s. [67 ALR 842](#) and [126 ALR 977](#); [14 ALR2d 234](#). An error of a judge is a clerical error where it is one which cannot reasonably be attributed to exercise of judicial consideration or discretion.”

N.C.G.S. § 47-36.1. Correction of errors in recorded instruments, provides:

Notwithstanding G.S. 47-14 and 47-17, an obvious typographical or other minor error in a deed or other instrument recorded with the register of deeds may be corrected by rerecording the original instrument with the correction clearly set out on the face of the instrument and with a statement of explanation attached. The parties who signed the original instrument or the attorney who drafted the original instrument shall initial the correction and sign the statement of explanation. If the statement of explanation is not signed by the parties who signed the original instrument, it shall state that the person signing the statement is the attorney who drafted the original instrument. The statement of explanation need not be acknowledged. Notice of the correction made pursuant to this section shall be effective from the time the instrument is rerecorded.

For example, in the case of [Green v. Crane](#), 96 N.C. App. 654, 386 S.E.2d 757 (1990), the “correction” of a legal description to add the additional language “*Being all of that certain tract or parcel of land more fully described in the Deed recorded in Book 135, Page 677, Avery County Registry, which property specifically includes*” ahead of an itemized listing of particular lots was not an “obvious typographical error” but was instead a purported addition of more property to the conveyance, an act which could only be done by correction by the signatories of the original instrument, not by the attorney unilaterally.

The conundrum: If the error is truly only “minor clerical”, obvious from review of the file, what is the purpose or necessity for correction by a non-party and rerecording? Should not the document itself, on its face, speak for itself with any minor issues resolved by a reading of the four corners of the instrument?

Corollary: If it is significant to require re-recording, is it truly just a “minor clerical” error at all? What circumstances would justify not returning to the parties for correction, re-execution and re-acknowledgment?

2. *If we do re-record, how do we re-establish a complete chain of title? (What is estoppel by deed anyway?) Oh, no – what about the new intervening lien they’ve recorded??????? What is the effective date of the “correction”?*

If the document is specific and complete enough to stand on its own and give sufficient record notice to later purchasers or mortgagees, then it was effective as of the time of initial recordation. In any situation involving a correction and re-recording that is substantial enough to necessitate a re-recording at all, at

best, the correction may be sufficient public notice only from the date of the re-recording. This is a very fact and judgment dependent analysis. And if the original recording document itself was not sufficient to validate the appropriate chain of title (thus, requiring re-recording), then any document in reliance on the validity and recordation of that document must also be recorded to be within the new corrected chain of title. This is especially the situation where the deed was erroneous and re-recordation was required for a substantial substantive notice issue, so that any deeds of trust from that grantee must also be re-recorded, whether by original deed of trust or certified copy of previously recorded deed of trust (where the error was solely in the deed).

3. *“Sorry, honey, we shredded the deed of trust”*

The clerical error correction statute is unavailable as a potential cure for a deed of trust containing an error if the original deed of trust cannot be retrieved and located. Though some have tried to "correct" a certified copy, once "corrected" (actually "defaced") by the notation on the face of the instrument itself, it is no longer either an original notarized document or even a certified copy of the previously recorded instrument and should be even be recordable.

Problem #9: Judgments & Federal Tax Liens: The Good, The Bad and The Ugly (Buyers, Sellers & Bankrupts)

1. *The buyer does not even have title yet? Why do I have to check the Clerk's office on them?*

Some key examples generating significant title claims and losses for innocent seller, purchasers and lenders:

- One co-tenant with significant tax liens, judgments or domestic problems can seriously impair the ability of all other co-tenants to finance, arrange construction and sell investment property. The situation is easily avoidable by noting the potential risk and changing the manner of vesting title.
- Vesting of property in purchaser's individual name creates issues for the purchaser and for the lender when spouse was incompetent or purchaser had unrelated judgments or tax liens and attorney has not advised of the effect of these interests on the property, including foreclosure or later sale or refinance.
- Purchaser had been declared legally incompetent and guardian appointed, with guardianship estate in active administration.
- Judgments in favor of the United States take priority over even purchase money liens, pursuant to the Federal Debt Collection Procedures Act of 1990 (28 U.S.C. 3201(b)).
- Purchase money priority is limited in situation involving purchase – construction loans, thus allowing the interests of pre-existing lien creditors of the borrower to take priority over post-closing construction advances. See Dalton Moran Shook, Inc. v. Pitt Dev. Co., 113 N.C. App. 707, 440 S.E.2d 585 (1994).

2. *But the property is held as tenants by the entirety? Why do I care if the husband has judgments or federal tax liens?*

Most individual judgments of just one spouse would not attach to real property held as tenants-by-the-entireties in North Carolina. However, the U.S. Supreme Court has carved out a huge exception with the case of United States v. Craft, 233 F.3d 358, reversed and remanded, 535 U.S. 274; 122 S. Ct. 1414 (Decided April 17, 2002). Fortunately, by Internal Revenue Bulletin: 2003-39 (September 29, 2003), Notice 2003-60: Collection Issues Related to Entireties Property, attached as Exhibit G, the Internal Revenue Service gave some assurance against enforcement actions for transactions with third party lenders and purchasers prior to April 2002. However, for property vested in the couple at any time (before or after April 2002) and still owned by the couple post-April 2002, whether or not they are still married, the individual federal tax liens of one of the (current or former) spouses will attach to the property and must be addressed in any transactions by them after April 2002, pursuant to the Notice.

Pursuant to Internal Revenue Bulletin 2003-39, Notice 2003-60 (September 29, 2003), "Collection Issues Related to Entireties Property" (available on-line at: http://www.irs.gov/irb/2003-39_IRB/ar13.html):

- "As a matter of administrative policy, . . . with respect to entireties property located in full bar jurisdictions [like North Carolina], the Service will not assert its federal tax lien priority over the interest of the class of persons protected under section 6323(a) [purchaser, holder of a security interest, mechanic's lienor or judgment lien creditor], if the section 6323(a) interests were created before Craft was decided" even if the federal tax lien against only one spouse was filed prior to the interest of the class of persons being created in the entireties property.
- "Divorce. A spouse of the taxpayer who obtained entireties property in a divorce acquires the property subject to the federal tax lien. In the context of a divorce, a spouse is not in the class of

persons protected by section 6323(a). Consequently, if the assessment giving rise to the federal tax lien under section 6321 had occurred prior to the divorce, then the lien also attached to the taxpayer's rights in the entirety property. As a general rule, if the transfer occurred before Craft, then the Service will treat the transfer as one for value and will not assert its lien against the property in the hands of the ex-spouse of the taxpayer. This will not apply if the Service determines that, notwithstanding the divorce, the transfer was fraudulent."

- "Entireties property subject to the federal tax lien and then transferred after Craft to a non-liable spouse pursuant to a divorce remains encumbered in the hands of the ex-spouse."
- NOTE: Even the above administrative decision does not change the result if the entirety property is held after divorce, converted to a tenancy in common and the filed federal tax lien attaches to the ½ interest of the taxpayer spouse. Similarly, if the taxpayer spouse dies while still married, the entirety property becomes the sole property of the surviving spouse, free of the taxpayer spouse's sole federal tax lien. If the non-taxpayer spouse dies while still married to the taxpayer, the entirety property becomes the sole property of the taxpayer spouse and the federal tax lien attaches to the entire interest.
- Property conveyed after Craft without a discharge of the lien will still, to the extent of a ½ undivided interest, be presumed subject to the lien.
- "[P]ursuant to section 7403, the district court has discretion to order the sale of the entire property, even where a non-liable spouse has a protected interest in the property. See United States v. Rodgers, 461 U.S. 677 (1983)."

Therefore, in any situation involving a federal tax lien against one or both spouses where property is or will be held in a tenancy by the entirety, most title companies will require the satisfaction and release of such liens, or discharge of the property from the liens, duly filed in the office of the Clerk of Superior Court in the applicable miscellaneous file(s), notwithstanding the fact that the title to the property is (or was, pre-divorce) held in the names of both spouses as tenants by the entirety.

IRS Form 8821 can be used to obtain release information on these or any other federal tax liens. The form is on-line at: <http://www.irs.gov/pub/irs-pdf/f8821.pdf>

3. *But these brothers and sisters inherited the property through an estate. Why can't we just pay as many of brother A's judgments as we can from his part and the rest of his creditors are out of luck?*

In the case of Drye v. United States, 152 F.3d 892, *aff'd* 528 U.S. 49 (Decided December 7, 1999), the United States Supreme Court determined that a federal tax lien against one son / heir attached to the potential interest he would have had under state law, even though he disclaimed the interest within time frame of state disclaimer statute. (This was the predecessor case strongly relied upon in the Craft case above.)

In addition, under NC law, it has long been the case that vested interests cannot be extinguished without due process. In the context of tenants in common, the liens of judgment creditors of one tenant in common cannot be extinguished (absent payment in full or voluntary release by the creditor) without their being joined in the partition action; or, in the alternative, the judgment remains attached as a lien to the property even after the partition absent joinder of the creditor and disposition of its lien interest through the partition action. Washburn v. Washburn, 234 N.C. 370, 67 S.E.2d 264 (1951).

4. *But I have a copy of the Order of Discharge? I thought bankruptcy extinguished all debts and liens?*

A judgment which attached to property prior to the filing of a bankruptcy proceeding will not be discharged by a general discharge of the debtor's *personal* liability. It simply becomes a nonrecourse lien on the property, not enforceable against the discharged debt but still a lien enforceable against subsequent owners and the property itself. It is similar to a purchase money deed of trust in being nonrecourse, but at least a purchase money deed of trust can be foreclosed against the borrower but no deficiency obtained. Compare, however, Property acquired *after* discharge is free and clear of the judgment lien since it did not attach prior to personal liability being discharged. Clowney v. North Carolina National Bank, 19 Bankr. 349 (Bankr. M.D.N.C. 1982).

LIST OF EXHIBITS

EXHIBIT A	Chicago Bull Edition 28 (Revised November 2003)
EXHIBIT B	NCTIRB Closing Protection Letter
EXHIBIT C	Flip Transactions – HUD Final Rules
EXHIBIT D	Open Estate Affidavit and Indemnity Agreement
EXHIBIT E	Owners Need Surveys – Still! (Or, <i>The Risks To You and Your Client</i> of Lender’s “Survey Coverage Without a Survey”)
EXHIBIT F	RPC 99, Title Insurance Tacking
EXHIBIT G	Internal Revenue Bulletin: 2003-39 (September 29, 2003) Notice 2003-60: Collection Issues Related to Entireties Property

EXHIBIT A



CHICAGO BULL

EDITION 28 (REVISED NOV 2003)

Closing Protection Letters in North Carolina: The New Procedure

Effective October 1, 2003, the North Carolina Department of Insurance has approved changes in form, procedure and cost of obtaining closing protection for North Carolina closings. (See attached announcement of the North Carolina Land Title Association.) By amended filing, effective November 3, 2003, notice shall be given that closing services insurance has or has not been provided. Chicago Title will assume that closing protection is desired on each transaction unless we are notified otherwise.

Why the change?

The modern real estate closing has become increasingly complex with more documents, more requirements, more parties, more variance among lender demands, more deadlines and less time to prepare than in the past. With this added pressure, comes the added risk of errors and losses, especially closing protection losses. Losses solely due to closing protection liability have escalated at an alarming rate to become a major source of losses for title companies.

What are closing protection losses as compared to traditional title coverage losses?

Historically, the attorney's certification of title would be the basis for requirements in a title insurance commitment. If the requirements were met, the policy would be issued as reflected by the commitment. If the requirements were not met, either additional exceptions would be taken in the policy or the policy would not be issued at all. "Closing protection" losses are the result of noncompliance with written closing instructions, some of which are *not title-related*, such as failure to deliver within specified deadlines:

- Clear well or septic tank report;
- Required lien priority status;
- Post-closing requirements;
- The closing package to the appropriate office of the lender; or
- The final lender title insurance policy and required endorsements.

Title coverage rates have been designed to provide adequate assurance of coverage of risks from *title* losses. This increase in *closing* losses was never included in a calculation of title rates. These losses are a product of the changes in closing process, documentation and time pressures.

What does this mean for the closing attorney and the client?

- (1) The approved form of Closing Protection Letter, specific to an identified attorney, borrower and lender, will be issued by complying companies. (Copy attached)
- (2) When closing services insurance is provided, a combined closing and title risk rate premium, a single undivided charge pursuant to N.C.Gen.Stat. §58-26-1(d), will be applicable. The closing services insurance portion of the premium shall be calculated as follows:

<u>Coverage</u>	<u>Per Thousand or Fraction thereof</u>
Up to \$100,000 of liability	\$0.50
\$100,001 to \$500,000, add	\$0.10

How do you find out more?

More specific information about the Rating Bureau and about the revised procedure is available on the web site of the North Carolina Department of Insurance – Industry -- Property and Casualty Insurance -- View Company Rate and Form Filings under the "North Carolina Title Insurance Rating Bureau" at:
Forms filing PC064747: <http://infoportal.ncdoi.net/filingdetail.jsp?fid=354848>
Rate filing PC064748: <http://infoportal.ncdoi.net/filingdetail.jsp?fid=354849>

And, of course, as always, feel free to contact your preferred office or agent of
Chicago Title Insurance Company

EXHIBIT B



Chicago Title Insurance Company

[Address]

Telephone: (000) 000-0000

Telecopier: (000) 000-0000

CLOSING PROTECTION LETTER

September 6, 2003

ATTENTION: JOHN SMITH
SAMPLE LENDER
123 WEST STREET
GREENVILLE, NC 23456-8765

Re: Borrower(s): BILLY BOB BUYER
Loan #: 2345-930187
Approved Attorney: SAMPLE ATTORNEY
1234 SAMPLE LANE
SAMPLE, NC 43256-9876

Dear Sir or Madam:

When title insurance of Chicago Title Insurance Company is specified for your protection in connection with closings of North Carolina real estate transactions in which you are to be the lessee or purchaser of an interest in land or a lender secured by a mortgage (including any other security instrument) of an interest in land in accordance with N.C. Gen. Stat. Sec. 58-26-1, the Company, subject to the Conditions and Exclusions set forth below, hereby agrees to reimburse you for actual loss incurred by you in connection with such closings when conducted by an Issuing Agent (an agent authorized to issue title insurance for the Company) or an Approved Attorney (an attorney upon whose certification of title the Company issues title insurance) and when such loss arises out of:

1. Failure of the Issuing Agent or Approved Attorney to comply with your written closing instructions to the extent that they relate to (a) the status of the title to said interest in land or the validity, enforceability and priority of the lien of said mortgage on said interest in land, including the obtaining of documents and the disbursements of funds necessary to establish such status of title or lien, or (b) the obtaining of any other document, specifically required by you, but only to the extent the failure to obtain such other document affects the status of the title to said interest in land or the validity, enforceability and priority of the lien of said mortgage on said interest in land, or
2. Fraud or dishonesty of the Issuing Agent or Approved Attorney in handling your funds or documents in connection with such closings to the extent such fraud or dishonesty relates to the status of the title to said interest in land or to the validity, enforceability, and priority of the lien of said mortgage on said interest in land.

If you are a lender protected under the foregoing paragraph, your borrower in connection with a loan secured by a mortgage on a one-to-four family dwelling shall be protected as if this letter were addressed to your borrower.

Conditions and Exclusions

- A. The Company will not be liable to you for loss arising out of:
 1. Failure of the Approved Attorney to comply with your closing instructions, which require title insurance protection inconsistent with that, set forth in the title insurance binder or commitment issued by the Company. Instructions that require the removal of specific exceptions to title or compliance with the requirements contained in said binder or commitment shall not be deemed to be inconsistent.

2. Loss or impairment of your funds in the course of collection or while on deposit with a bank due to bank failure, insolvency or suspension, except such as shall result from failure of the Issuing Agent or the Approved Attorney to comply with your written closing instructions to deposit the funds in a bank which you designated by name.
 3. Mechanics' and materialmen's liens in connection with your purchase or lease or construction loan transactions, except to the extent that a title insurance binder, commitment or policy of the Company affords protection against such liens.
 4. Failure of the Issuing Agent or Approved Attorney to comply with your written closing instructions to the extent such instructions require a determination by the Issuing Agent or Approved Attorney of the validity, enforceability or effectiveness of any document contemplated under paragraph 1(b) above.
- B. If the closing is to be conducted by an Issuing Agent or an Approved Attorney, a title insurance binder or commitment for the issuance of a policy of title insurance of the Company must have been received by you prior to the transmission of your final closing instructions to the Issuing Agent or Approved Attorney.
 - C. When the Company shall have reimbursed you pursuant to the coverage contained in this letter, it shall be subrogated to all rights and remedies, which you would have had against any person or property, had you not been so reimbursed. Liability of the Company for such reimbursement shall be reduced to the extent that you have knowingly and voluntarily impaired the value of such right of subrogation.
 - D. Any liability of the Company for loss incurred by you in connection with closings of real estate transactions by an Issuing Agent or Approved Attorney shall be limited to the coverage provided. However, this coverage shall not affect the protection afforded by a title insurance binder, commitment or other policy of the Company.
 - E. Claims shall be made promptly to the Company at its principal office at 171 North Clark Street, Chicago, Illinois 60601. When the failure to give prompt notice shall prejudice the Company, then liability of the Company hereunder shall be reduced to the extent of such prejudice. The Company shall not be liable hereunder unless the Company receives notice of claim in writing within three years from the date of the Closing.
 - F. The coverage herein offered extends only to real property transactions in North Carolina.

The coverage herein offered will be effective upon your disbursement of funds to the Issuing Agent or Approved Attorney identified above after you receive this letter and will continue until canceled by written notice from the Company.

Any previous Closing Protection Letter or similar agreement is hereby canceled, except as to closings of your real estate transactions regarding which you have previously sent (or within 30 days hereafter send) written closing instructions to the Issuing Agent or Approved Attorney.

Chicago Title Insurance Company

By: _____ S A M P L E
Authorized Agent

Re: Borrower(s): BILLY BOB BUYER

EXHIBIT C

Chicago Title Insurance Company – Flip Transactions – HUD Final Rules

DATE: May 30, 2003

The Department of Housing and Urban Development (HUD) has issued a final rule intended to prohibit "flipping" in HUD's Single Family Mortgage Insurance Program. The rule takes effect June 2, 2003. A copy is attached.

The new rule defines flipping as "the predatory lending practice whereby a property recently acquired is resold for a considerable profit with an artificially inflated value, often abetted by a lender's collusion with the appraiser."

To obtain FHA mortgage insurance of a buyer's mortgage, lenders will now have to consider:

1. the "acquisition" date, being the date on which seller acquired title to the property (being the date of settlement and not the recording date of the deed);
2. the "re-sale" date, being the date on which the buyer/borrower signs a contract to purchase the land;
3. the price at which the seller acquired the land; and
4. the price at which the buyer/borrower will purchase the land.

In sum, the new rule operates as follows:

First, if the re-sale date is 90 days or less following the date of acquisition by the seller, the property is *not* eligible for FHA mortgage insurance. See exceptions below.

Second, If the re-sale date is between 91 days and 180 days following the date of acquisition by seller, then the property is generally eligible for FHA mortgage insurance, except that lender will be required to submit to HUD additional documentation to support the value of the re-sale price if the re-sale price is 100 percent greater than the seller's acquisition price. The additional documentation must include an additional appraisal or evidence of rehabilitation or improvement to the property. The 100 percent figure is not a fixed number. HUD may adjust the number from time to time within the range of 50 percent to 150 percent. Same exceptions as in first paragraph; see below.

Third, if the re-sale date is more than 90 days after date of acquisition by seller but less than 12 months after date of seller's acquisition, then the property is eligible for FHA mortgage insurance, except that lender must provide HUD with additional information to support the re-sale value of the property "if the re-sale price is 5 percent or greater than the lowest sales price of the property during the preceding 12 months." (I have read the quoted words about 15 times now and still can't figure out what is meant; lenders will have to interpret the words, not us.) HUD may remove sales prices below a certain dollar amount from this provision, but the new rule does not set any such dollar amount. Same exceptions as under first and second paragraphs; see below.

The following transactions are the only exceptions to all three of the above paragraphs: re-sales by HUD of REO and similar properties; and re-sales of properties purchased by an employer or relocation agency in connection with the relocation of an employee.

Finally, the HUD rule imposes an "owner of record" requirement. To be eligible for FHA mortgage insurance, the property must be purchased from the owner of record. The transaction may not involve

any sale or assignment of the purchase contract. Lender must submit to HUD documentation verifying that seller is the record owner. A title commitment may be used for this purpose.

EXHIBIT D
CHICAGO TITLE INSURANCE COMPANY
OPEN ESTATE AFFIDAVIT AND INDEMNITY AGREEMENT

NOTE: THIS FORM IS TO BE USED ONLY IN SITUATIONS WHICH HAVE BEEN SPECIFICALLY
APPROVED BY AN UNDERWRITER FOR CHICAGO TITLE INSURANCE COMPANY PRIOR TO CLOSING

This **AFFIDAVIT AND INDEMNITY AGREEMENT** (hereinafter "Agreement") made and entered into as of the _____ day of _____, 20____, by and between _____

_____ (collectively, and jointly and severally if more than one, hereinafter "Indemnitor"), and CHICAGO TITLE INSURANCE COMPANY (hereinafter "Company").

WITNESSETH:

WHEREAS, Company has been asked to issue its title insurance commitment(s) and/or policy or policies insuring against loss or damage by reason of defects or possible defects in the title to property described as follows (hereinafter "Property"):

WHEREAS, the Property was formerly owned by:

Decedent: _____
Date of Death: _____
Estate File No: _____
County: _____ ; and

WHEREAS, Decedent's estate has not been fully administered and closed; and

WHEREAS, title to the Property has passed under Decedent's will admitted to probate or pursuant to the laws of intestacy to the following parties (please indicate if minor or incompetent): _____

_____ ; and

WHEREAS, _____ has been appointed by the Clerk of Superior Court as _____ Executor _____ Administrator of Decedent's estate; and

WHEREAS, if Decedent died within the preceding two years, the Notice to Creditors has been published at least once; and

WHEREAS, Company has noted as exceptions to the aforesaid title the following actual or supposed rights, interests, liens, claims, encumbrances or defects in title (hereinafter "Title Matter"):

The Property is or may be subject to matters resulting from the incomplete administration of Decedent's estate including but not limited to: any debts or claims of debt of the estate of Decedent; potential estate and/or inheritance taxes; appeal of any order admitting a will to probate; institution of a suit impeaching such will; filing of a claim for an elective share; filing of a renunciation of any interests in property; discovery and probate of a later will; claims or interests of any undisclosed or disinherited heirs or undisclosed spouses of

heirs or devisees; disqualification of any heir or devisee of Decedent's estate; and any claim of unmarketability of title.

WHEREAS, Indemnitor desires Company issue its title insurance commitment(s) and/or policy or policies without exception to or providing affirmative coverage for the Title Matter; and

WHEREAS, Company may concurrently herewith or hereafter in the ordinary course of its business issue another commitment and/or policy in the form or forms now or then commonly used by Company insuring without exception to or providing affirmative coverage for the Title Matter; and

WHEREAS, Company is willing to issue its commitment(s) and/or policy or policies without exception to or providing affirmative coverage for the Title Matter only if indemnified as herein set out.

NOW, THEREFORE, for and in consideration of the issuance of said title insurance commitment(s) and/or policy or policies and other good and valuable consideration, the receipt of which is hereby acknowledged, Indemnitor does hereby agree with Company as follows:

1. Indemnitor agrees to defend, at Indemnitor's own cost and expense on behalf of and for the protection of Company and the parties insured or who may be insured under said title insurance commitment(s) and/or policy or policies (but without prejudice to the right of Company to defend at the reasonable expense of Indemnitor if it so elects), any and every suit, action or proceeding in which the Title Matter may be asserted or attempted to be asserted, established or enforced in, to, upon, against or in respect to the Property, or any part thereof, or interest therein.
2. Indemnitor agrees to indemnify and hold Company and any parties insured or who may be insured under said title insurance commitment(s) and/or policy or policies harmless of and from any and all loss, costs, damage and expense of every kind, including attorney's fees, which Company and/or said parties shall or may incur or become liable for as a result of the Title Matter, directly or indirectly, including but not limited to diminution in value, unmarketability of title and actions to enforce this Agreement.
3. Each and every provision of this Agreement shall extend to and be in force concerning any and every other title insurance commitment and/or policy Company may at any time or times hereafter issue insuring without exception to or providing affirmative coverage for the Title Matter.
4. This Agreement contains the entire agreement of the parties and there are no representations, inducements, or other provisions other than those expressed in writing. All changes, additions or deletions hereto must be in writing and signed by all parties.
5. This Agreement shall be governed by and construed in accordance with the laws of the State of North Carolina . It is made to induce the purchase of and/or a loan secured by the Property described herein and the issuance of a title insurance commitment(s) and/or policy or policies relating to same. Indemnitor acknowledges that Company is relying on the representations and indemnifications contained herein in issuance of said commitment(s) and/or policy or policies. The provisions of this Agreement shall survive the disbursement of funds and closing of this transaction and shall be binding upon Indemnitor, its/their successors and/or assigns.
6. Indemnitor agrees that the Company may demand arbitration pursuant to the Commercial Arbitration Rules of the American Arbitration Association. Arbitrable matters may include, but are not limited to, any controversy or claim between the Company and the Indemnitor arising out of or relating to this Agreement, or any breach thereof. Arbitration pursuant to this Agreement and under the Rules in effect on the date of this Agreement, shall be binding upon the parties. Judgment upon the award rendered by the Arbitrator(s) may be entered in any court having jurisdiction thereof.

IN WITNESS WHEREOF, this Agreement is executed as of the day and year first above written.

ENTITY NAME

By: _____
Printed/Typed Name: _____
Title: _____

By: _____
Printed/Typed Name: _____
Title: _____

Entity Address: _____
Tax Identification No. _____

STATE OF _____ COUNTY OF _____

Sworn to and subscribed before me this the _____
day of _____, 20____.

Notary Public

My Commission Expires: _____

Notary Seal

Printed/Typed Name: _____
Address: _____
Social Security No. _____

Printed/Typed Name: _____
Address: _____
Social Security No. _____

Printed/Typed Name: _____
Address: _____
Social Security No. _____

Printed/Typed Name: _____
Address: _____
Social Security No. _____

EXHIBIT E



CHICAGO BULL
VOLUME 1, EDITION 5

Owners Need Surveys – Still!

(Or, The Risks To You and Your Client of Lender’s “Survey Coverage Without a Survey”)

You have heard it a hundred times. In gathering information about a closing, you ask either the real estate broker or the owner about whether you should obtain a survey. Their response: “My broker told me I do not have to have a survey. The title insurance company will cover it.” To assist in lowering costs, the practice of providing lender’s coverage without a new survey was developed in residential transactions. In the absence of a current survey, the customary practice is to issue the loan policy without a survey exception. And now this has expanded into *commercial properties (under \$5 million) as well!*

But the owner will not be covered, even in those situations where the lender might be! The owner’s policy contains an exception for easements, setbacks and other matters which would have been shown on a survey.

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!* In many of these cases, the lender could have avoided delinquencies and other problems if they, too, had obtained an actual survey to identify problems at or before closing.

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 which 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 a good title policy coverage on) Lot 1 of Happy Homes Subdivision. Unfortunately the house they thought they bought was on Lot 2. And 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 *demand*s 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 which 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.

The surveyor is a critical link between your legal assessment of title and the actual “dirt” your client believes they are purchasing. The surveyor can save you and your client untold misery in the future. Many of the above cases have also caused losses to lenders, due to delays in foreclosures, joinder as necessary parties in lawsuits or disruptions in their borrowers' desire to make payments pending resolution of problems, often not covered by their title policies because not purely *title* problems.

So, the next time your owner says “my broker told me . . .,” perhaps you'll have a few more examples to add to your stock of advice to them! And maybe a “Waiver of Survey Affidavit” such as the attached might be in order!

Happy Closings!

Chicago Title Insurance Company

STATE OF NORTH CAROLINA
COUNTY OF _____

AFFIDAVIT REGARDING WAIVER OF SURVEY

BUYERS: _____
CLOSING ATTORNEY: _____
PROPERTY: _____

The undersigned Buyers of the Property above do hereby certify as follows:

1. The Buyers have been generally advised by the Closing Attorney of the reasons for obtaining a current survey of the Property.
2. The Closing Attorney has disclosed the potential risk of not obtaining a current survey on behalf of the Buyers, including but not limited to, the following risks:
 - If a prior survey exists or has been provided, that surveyor may have no liability to the Buyers for any inaccuracies in this prior survey.
 - The Buyers' new title insurance policy (if any) may not provide full current owner's survey coverage, and
 - The Buyers may have no protection against or notice of matters which a current survey might reveal, many of which are not matters of public record and would not be included in an attorney's title opinion.
3. The Buyers are aware that failure to remedy or obtain insurance to cover problems a survey might reveal may result in financial loss to them in the future, for which they may not be insured.
4. After considering this information, the undersigned Buyers choose to waive the option of obtaining a current survey.
5. The Buyers hereby agree to hold the Closing Attorney and Chicago Title Insurance Company harmless from any loss or damage resulting from matters which would be revealed by a current survey, including but not limited to court costs and attorneys' fees.

This the ____ day of _____, 2000.

Buyer / Owner

Buyer / Owner

Sworn to and subscribed before me,
This the ____ day of _____, 200__.

Notary Public

My Commission Expires: _____

EXHIBIT F

RPC 99 (April 12, 1991)

[From the North Carolina State Bar, www.ncbar.com]

Editor's Note: This opinion was originally published as RPC 99 (Revised).

Title Insurance Tacking

Opinion rules that a lawyer may tack onto an existing title insurance policy.

Inquiry #1:

In 1986, Lawyer A represented Mr. Jones in his purchase of a house and lot. A performed a full title search and obtained a title insurance policy for Jones and his lender with Title Insurance Company. In 1990, Jones contracts to sell the house and lot to Ms. Smith. Smith retains Lawyer B to represent her in the transaction. B obtains a copy of the policy Title Insurance Company issued on the property.

Lawyer B's title search for Smith consists of updating Lawyer A's search; B searches the title from 1986 to 1990.

Title Insurance Company allows B to apply for title insurance based on the update, and holds A liable for any title defects during A's search period that result in a claim against Smith. A never represented Smith. A has no

knowledge that A's work is serving as the basis for providing title insurance to Smith. Title company has never informed A that A's liability to title company extends beyond the time A's clients owned the property. Lawyer B has made no attempt to obtain A's permission to use A's base title.

May Lawyer B render a title opinion without having conducted a personal inspection of documents in the chain of title?

Opinion #1:

Yes. A lawyer may ethically render to a title insurance company a limited title opinion based upon a limited examination of the public records for the purpose of obtaining the issuance of a title insurance policy upon real property. The Rules of Professional Conduct do not require personal inspection of all documents in the chain of title so long as the lawyer rendering the opinion fully discloses to his or her client the precise nature of the service being rendered and the full extent thereof. The client should be advised that he or she should rely on the title insurance policy as to matters of title and not upon the attorney's examination of the public records. If the Title Insurance Company is willing to base its underwriting decision upon the fact that it or another title insurance company has previously issued a title insurance policy and Lawyer B's limited title opinion, that does not offend the Rules of Professional Conduct.

Since title insurers frequently omit exceptions in mortgagees' policies that would appear in owners' policies, tacking should be limited to tacking onto owners' policies.

Inquiry #2:

May Lawyer B tack onto Lawyer A's base title without first obtaining Lawyer A's permission?

Opinion #2:

Lawyer B may ethically apply for the issuance of a title insurance policy on the basis of her limited title opinion and the fact that a title insurance policy has previously been issued. In so doing, the Rules of Professional Conduct would not require Lawyer B to obtain Lawyer A's permission. It is a question of law as to whether or not Lawyer A's liability to the title insurance company would continue after the issuance of the new policy. It is beyond the purview of this committee to make that determination. A possible solution to this problem might be for a lawyer to include in her opinion to the title insurer a disclaimer to the effect that the opinion is submitted only with respect to the current transaction and is not to be relied upon in any future transaction.

Inquiry #3:

Must Lawyer B disclose to his or her client that B has updated the title and not performed a full title search? Must the disclosure be in writing? Must the disclosure be made before the client agrees to engage Lawyer B?

Opinion #3:

The disclosures referred to in the first opinion should be made by Lawyer B to the client prior to accepting employment. Rule 6(b)(2). The disclosures need not be in writing.

EXHIBIT G

Internal Revenue Bulletin

http://www.irs.gov/irb/2003-39_IRB/ar13.html

Internal Revenue Bulletin: 2003-39
September 29, 2003

Notice 2003-60
Collection Issues Related to Entireties Property

Table of Contents

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OVERVIEW
QUESTIONS AND ANSWERS

PURPOSE

This notice provides guidance on collection from property held in a tenancy by the entirety, where only one spouse (referred to here as the taxpayer) is liable for the outstanding taxes, in light of the Supreme Court decision in *United States v. Craft*, 535 U.S. 274 (2002).

BACKGROUND

On April 17, 2002, the Supreme Court issued its decision in *United States v. Craft*, 535 U.S. 274 (2002) (2002-38 I.R.B. 548), and held that the federal tax lien that arises under section 6321 of the Internal Revenue Code on “all property and rights to property” of a delinquent taxpayer attaches to the rights of the taxpayer in property held as a tenancy by the entirety (entireties property), even though local Michigan law insulates entireties property from the claims of creditors of only one spouse. The Court stated that while state law determines what rights a taxpayer has in property, federal law determines whether the state-defined rights are “property” or “rights to property” for purposes of section 6321. The Court’s decision in *Craft* has consequences in the approximately twenty-six jurisdictions that recognize tenancy by the entirety as a form of property ownership.

While state law governing property ownership varies by jurisdiction, there are a number of principles generally applicable to a tenancy by the entirety. Tenancy by the entirety is a form of property ownership, including personal property in some jurisdictions, available only to a husband and wife as a marital unit. A key feature of the tenancy is the right of survivorship—the surviving spouse becomes the fee simple owner of the property upon the death of the other spouse. The tenancy also is terminated by the transfer of the property or upon the spouses’ divorce.

Entireties property is subject to the claims of the joint creditors of the spouses. However, the majority of jurisdictions that recognize tenancy by the entirety, so-called full bar jurisdictions, completely prohibit creditors from attaching entireties property to satisfy the debts of only one spouse. The state law rationale is that a spouse individually has no interest in the property; rather, the property is held by the marital unit. The other jurisdictions that recognize tenancy by the entirety, so-called modified or partial bar jurisdictions, permit creditors to attach one spouse’s interest in entireties property for the debts of only that spouse, subject to the rights of the non-liable spouse.

Issues related to entireties property can arise in a number of areas, including enforcing collection through administrative and judicial means, evaluating offers in compromise and proposed installment agreements, valuing the Service’s secured claim in bankruptcy, applications for discharge and subordination, and determining the nature of the Service’s rights vis-a-vis a transferee in a transfer in which the federal tax lien has not been discharged.

OVERVIEW

The Service will rely on a number of general principles in addressing issues raised as a result of the Court’s decision in *Craft*:

(1) Under section 6321, the federal tax lien attaches to all the property and rights to property of the taxpayer. The Court's decision confirms that, for purposes of section 6321, a taxpayer's property and rights to property have always included any rights that taxpayer may have in entireties property under state law. The Court's decision, therefore, does not represent new law and does not affect other law applicable to federal tax liens and federal tax collection. For example, the Craft decision does not change any limitation on the ability of the Service to rescind an accepted offer in compromise or terminate an accepted installment agreement.

(2) As a matter of administrative policy, the Service will, under certain circumstances, not apply Craft, with respect to certain interests created before Craft, to the detriment of third parties who may have reasonably relied on the belief that state law prevents the attachment of the federal tax lien.

(3) The administrative sale of entireties property subject to the federal tax lien presents practical problems that limit the usefulness of the Service's seizure and sale procedures. Levying on cash and cash equivalents held as entireties property is considerably less problematic and will be used by the Service in appropriate cases.

(4) Because of the potential adverse consequences to the non-liable spouse of the taxpayer, the use of lien foreclosure for entireties property subject to the federal tax lien will be determined on a case-by-case basis.

(5) As a general rule, the value of the taxpayer's interest in entireties property will be deemed to be one-half.

(6) Where there has been a sale or other transfer of entireties property subject to the federal tax lien that does not provide for the discharge of the lien, whether the transfer is to the non-liable spouse or a third party, the lien thereafter encumbers a one-half interest in the property held by the transferee.

QUESTIONS AND ANSWERS

The following questions and answers illustrate how the Service will apply Craft. The first two Q&As address the application of Craft with respect to interests in entireties property acquired before the date of the decision, while the remaining questions and answers address its application with respect to interests acquired after the date of the decision.

Q1. If the Service has filed a notice of federal tax lien with respect to the taxpayer before Craft and an interest in entireties property was later acquired by a purchaser, a holder of a security interest, a mechanic's lienor, or a judgment lien creditor within the meaning of section 6323, then will the Service assert lien priority over the subsequently acquired interest? What if the entireties property was transferred, before Craft, to the non-taxpayer spouse in a divorce? Does the result differ if, before Craft, the transfer was to a donee, such as a family trust? Do the results differ depending on whether the jurisdiction at issue is one that recognizes tenancy by the entirety and completely prohibits the attachment of entireties property for separate debts of one spouse (i.e., a full bar jurisdiction) or one that permits attachment to entireties property in connection with the separate debts of one spouse (i.e., a modified or partial bar jurisdiction)?

A1. Application of Section 6323. Section 6323 provides that "[t]he lien imposed by section 6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof which meets the requirements of subsection (f) has been filed by the Secretary." Section 6323(a). The rule of Craft, with respect to entireties property, applies to federal tax liens regardless of when they arose. A federal tax lien, therefore, has priority over any interest of a purchaser, a holder of a security interest, a mechanic's lienor, or a judgment lien creditor (i.e., the class of persons protected by section 6323(a)) if notice of the federal tax lien was filed before such other interest arose.

As a matter of administrative policy, the Service will not assert its federal tax lien rights where doing so may disturb the settled expectations of certain classes of persons who may have been under the belief that a federal tax lien arising from the liability of only one spouse does not attach to entireties property. Accordingly, with respect to entireties property located in full bar jurisdictions, the Service will not assert its federal tax lien priority over the interests of the class of persons protected under section 6323(a), if the section 6323(a) interests were created before Craft was decided. For example, if a purchaser acquired entireties property before Craft was decided and meets the

definition of a purchaser under section 6323(h)(6), the Service will not assert lien priority even though a notice of federal tax lien had been filed prior to the purchase.

In contrast to full bar jurisdictions, there are no settled expectations in modified or partial bar jurisdictions, where a creditor is permitted to attach some or all of a debtor-spouse's interest in entireties property. For example, while Oklahoma law recognizes tenancy by the entireties as a form of property ownership, creditors collecting the debt of one spouse can force the sale of entireties property, severing the tenancy. In modified or partial bar jurisdictions, the Service will assert its lien priority against the class of persons protected under section 6323(a) regardless of when those persons may have acquired interests in entireties property, so long as those interests were acquired after a notice of federal tax lien had been filed.

Divorce. A spouse of the taxpayer who obtained entireties property in a divorce acquires the property subject to the federal tax lien. In the context of a divorce, a spouse is not in the class of persons protected by section 6323(a). Consequently, if the assessment giving rise to the federal tax lien under section 6321 had occurred prior to the divorce, then the lien also attached to the taxpayer's rights in the entireties property. As a general rule, if the transfer occurred before Craft, then the Service will treat the transfer as one for value and will not assert its lien against the property in the hands of the ex-spouse of the taxpayer. This will not apply if the Service determines that, notwithstanding the divorce, the transfer was fraudulent.

Donation. A donee who obtains entireties property acquires the property subject to the federal tax lien. As in the case of a transfer pursuant to a divorce, the donee is not in the class of persons protected by section 6323(a). Transfers to donees that occurred before Craft will be evaluated on a case-by-case basis to determine whether the equities favor or disfavor the Service asserting the federal tax lien against property held by a donee. There may be circumstances where, although the donee gave nothing of value in exchange for the property, it would be inequitable for the Service to assert the federal tax lien because of the donee's reliance on the mistaken view that the property was unencumbered. For example, if the transfer was of real property to which the donee has made substantial improvements, the equities may favor not asserting the federal tax lien (or agreeing to limit its reach by carving out the value of the improvements). On the other hand, the absence of such reliance may warrant assertion of the federal tax lien.

The identity of the donee is also a factor that will be considered by the Service. The federal tax lien is more appropriately not asserted where the donee is a disinterested person, having no relation to the taxpayer, than where the donee and taxpayer are closely related. For example, the Service may decide to assert the federal tax lien where the taxpayer transferred entireties property to a family trust, but may decide not to assert the lien where the taxpayer transferred entireties property to a charitable organization.

Q2. Does the Craft decision provide a basis for the Service to rescind offers in compromise, terminate installment agreements, or revoke certificates of discharge and subordination? Will the Service amend bankruptcy proofs of claim? Can the Service revisit a determination that an account is currently not collectible?

A2. The decision in Craft does not provide legal authority to rescind any accepted offer in compromise, terminate an installment agreement, or revoke any certificate of subordination or discharge.

With respect to bankruptcy proofs of claim, the Service has made an administrative decision not to routinely amend such proofs of claim to adjust the amount of the Government's secured claim to reflect the federal tax lien on the taxpayer's interest in entireties property. There may be circumstances, however, where the Service elects to amend the claim to assert the federal tax lien on entireties property, depending on the value of the property and the status of the bankruptcy case. The existence of entireties property will be considered in filing new proofs of claim and in future investigations related to determining whether there is any property subject to post-bankruptcy collection.

Finally, based on an evaluation of a taxpayer's interest in entireties property, the Service may revisit a prior determination that an account is currently not collectible.

Q3. If entireties property subject to the federal tax lien is sold or transferred after Craft and the Service does not discharge the lien, is the property subject to the federal tax lien in the hands of the transferee?

A3. A conveyance of entireties property terminates the entireties estate with respect to that property. Accordingly, after Craft, unless the Service discharges the property from the federal tax lien, the lien will encumber a one-half interest in the hands of the transferee, regardless of whether the transferee is a donee or gives value. As explained below, the Service generally will deem the value of the taxpayer's interest in entireties property to be one-half of the total value of the property.

Q4. Does the federal tax lien on entireties property survive the death of the taxpayer? What effect does the death of the non-taxpayer have on the federal tax lien?

A4. As is the case with joint tenancy with the right of survivorship, if a taxpayer's interest in entireties property is extinguished by operation of law at the death of the taxpayer, then there is no longer an interest of the taxpayer to which the federal tax lien attaches. When a taxpayer dies, the surviving non-liable spouse takes the property unencumbered by the federal tax lien.

When a non-liable spouse predeceases the taxpayer, the property ceases to be held in a tenancy by the entirety, the taxpayer takes the entire property in fee simple, and the federal tax lien attaches to the entire property.

The rule that the federal tax lien does not survive the death of the taxpayer does not apply if the entireties estate previously has been terminated. For example, if the property has been conveyed to a third party, the federal tax lien will be deemed to encumber a one-half interest in the hands of the transferee and will not be affected by the subsequent death of either spouse.

Q5. Does the federal tax lien remain on entireties property awarded to a non-liable spouse in a divorce decree?

A5. Entireties property subject to the federal tax lien and then transferred after Craft to a non-liable spouse pursuant to a divorce remains encumbered in the hands of the ex-spouse.

Q6. After a notice of federal tax lien is filed, the taxpayer and spouse jointly mortgage entireties property to a bank. What effect would the death of either spouse have on the respective rights of the Government and the bank? Where the property is transferred either to a third party or as a result of a divorce, does the federal tax lien have priority over the bank?

A6. Under section 6323, the federal tax lien has priority over the bank's interest with respect to the taxpayer's interest in the entireties property.

If the taxpayer survives the spouse, the federal tax lien will be a senior lien against the whole property. The taxpayer's interest in the entireties property to which the federal tax lien attaches includes the taxpayer's right of survivorship. With the death of the taxpayer's spouse, the taxpayer becomes the fee simple owner of the property, and the federal tax lien attaches to that interest in the property, which is senior to the bank's interest.

As discussed in Q&A 4, if the taxpayer predeceases the spouse and his or her interest is extinguished by operation of law, the federal tax lien will be extinguished. The mortgage lien becomes the first lien on the property.

Since a divorce or transfer to a third party terminates the entireties estate (and, with it, the spouses' rights of survivorship), if the property is transferred to a third-party or to either spouse as a result of a divorce, then the federal tax lien generally will have priority with respect to a one-half interest in the property over the bank's subsequent security interest.

Q7. Will the Service administratively seize and sell the taxpayer's interest in entireties property?

A7. The Service can administratively seize and sell a taxpayer's interest in real and personal property held in a tenancy by the entirety. Because of the nature of entireties property, it would be very difficult to gauge what market there would be for the taxpayer's interest in the property. The amount of any bid would in all likelihood be depressed to the extent that the prospective purchaser, given the rights of survivorship, would take the risk that the

taxpayer may not outlive his or her spouse. In addition, a prospective purchaser would not know with any certainty if, how, and the extent to which the rights acquired in an administrative sale could be enforced. For example, rights acquired would include the right to use the property and the right to exclude others from the property. It is not clear how the rights of a prospective purchaser ultimately would be balanced with the co-existing rights of the spouse of the taxpayer. Therefore, the Service has determined that an administrative sale is not a preferable method of collection with respect to entireties property.

Levying on cash and cash equivalents held as entireties property does not present the same impediments as seizing and selling entireties property. For example, where the Service levies on a bank account that a taxpayer holds as entireties property and has the right to withdraw the funds in the account, the bank is obligated to turn over the funds in response to the levy. While the taxpayer's spouse, as the other account holder, may have an administrative or judicial claim under sections 6343(b) or 7426, respectively, see *United States v. National Bank of Commerce*, 472 U.S. 713 (1985), the amount realizable by the Service is not, at the outset, depressed as it is in the case of administrative sales.

Q8. Will the Service foreclose the federal tax lien against entireties property?

A8. The Service will foreclose the federal tax lien against entireties property in appropriate cases. While in an administrative sale the Service can sell only the taxpayer's interest in entireties property (i.e., not the entire property itself), in a foreclosure action, pursuant to section 7403, the district court has discretion to order the sale of the entire property, even where a non-liable spouse has a protected interest in the property. See *United States v. Rodgers*, 461 U.S. 677 (1983) (principle applied with respect to the sale of homestead property). If the court orders the sale of the property, then the non-liable spouse must be compensated for his or her interest: section 7403 requires "a distribution of the proceeds of such sale according to the findings of the court in respect to the interests of the parties and the United States." Section 7403(c).

Q9. How is the Government's federal tax lien interest in entireties property valued for the purposes of discharge and subordination under section 6325? After private foreclosure on entireties property, what is the value of the Government's interest in proceeds left after the satisfaction of senior liens? How is entireties property valued for bankruptcy purposes? How is entireties property valued in offers in compromise?

A9. Discharge and Subordination. Under section 6325(b)(2)(A), the Service may issue a certificate of discharge of property subject to a federal tax lien upon payment of an amount not less than the value of the Government's interest in that property to be discharged. If a taxpayer applies for a certificate of discharge when entireties property is to be sold by the taxpayer and the taxpayer's spouse, then the taxpayer generally must pay the Service one-half the proceeds of the sale in partial satisfaction of the liability secured by the federal tax lien.

Foreclosing mortgagees with interests that are senior to the federal tax lien often seek a certificate of discharge, rather than joining the United States in a judicial proceeding. By obtaining a discharge of the mortgaged property, the mortgagee eliminates the Service's right under section 2410(c) of Title 28 to redeem the property from the purchaser after the foreclosure sale. As in the case of a taxpayer who seeks a certificate of discharge of the entireties property, the Service generally will determine the value of the Government's interest to be one-half the value of the property, which is determined for this purpose by first taking into account the amount of senior liens.

Under 6325(b)(4), an owner of property subject to a tax lien (for example, a subsequent purchaser), other than the taxpayer whose liability gave rise to the lien, may seek a certificate of discharge by making a deposit or posting a bond equal to the value of the interest of the Government in the property. In connection with an application for discharge of former entireties property under section 6325(b)(4), the Service generally will determine the value of the Government's interest to be one-half the value of the property.

In light of the Craft decision, taxpayers and taxpayers' spouses will seek subordination of the federal tax lien in connection with refinancing mortgages on entireties property. If the requested subordination is for the purpose of securing a loan to refinance a senior lien, the Service will apply section 6325(d)(2). The Service will generally issue a certificate of subordination if the terms of the refinance loan, as compared to the terms of the loan secured by the

senior lien, ultimately will enhance the taxpayer's equity or facilitate the collection of the tax from other property or income of the taxpayer.

If a taxpayer and a taxpayer's spouse seek a certificate of subordination for the purpose of obtaining cash or paying other debts not secured by a senior lien on the property (for example, in the case of a home equity loan), the Service will apply section 6325(d)(1). The Service generally will treat the value of the taxpayer's interest as one-half of the value of the entireties property. The Service would issue a certificate of subordination upon payment of one-half the amount of the lien or interest to which the federal tax lien will be subordinated.

Private Foreclosure. Where a senior creditor is foreclosing a mortgage or other lien on the property, the Service generally will determine the value of the taxpayer's interest to be one-half of the excess of the value of the property over the amount of the senior lien.

Bankruptcy. In bankruptcy cases, the Service, in determining the value of its secured claim, generally will value the debtor's interest in entireties property to be one-half of the total value of the property.

Offers in Compromise. Procedures for valuing entireties property for offer in compromise purposes are set forth in the Offer in Compromise Handbook, IRM 5.8.5.3.11.

The principal author of this notice is Deborah Grogan of the Office of Associate Chief Counsel (Procedure and Administration). For further information regarding this notice, contact Ms. Grogan at (202) 622-3610 (not a toll-free call).