THE NC CONNECTION

AN INVESTORS TITLE COMPANY PUBLICATION

Warranties of Title:

Estoppel by Deed vs. the Connor Act

by W. A. Foley, III, VP-Title Attorney
Click here for Drew's Bio
dfoley@invtitle.com

The general warranty deed commonly used to transfer title in residential real estate transactions contains covenants and warranties of title that protect the purchaser. These covenants and warranties preceded the enactment of recording statutes and were the first form of protection or warranty of title. The advent of recording statutes, like the Connor Act, gave a purchaser the ability to rely on the public record for an additional assurance of title. The warranties of title and the recording act usually work together to protect the purchaser — sometimes, however, their synergy creates a conflict. The common law doctrine of estoppel by deed and the dictates of the Connor Act, which is deemed to create a "pure race" to the courthouse, can give rise to such a conflict.

> "The doctrine of estoppel by deed originates in the covenant of warranty of title."

The doctrine of estoppel by deed originates in the covenant of warranty of title. This covenant of warranty indemnifies the grantee that the grantor has title to the real property conveyed, that there are no outstanding interests existing at the time of the conveyance, and that the grantor will defend the title of the grantee against all valid claims in the future. Thus, the covenant is a promise, an assurance, and an indemnification. The covenant of warranty, however, will also cause an estoppel if the grantor ever asserts superior title over his grantee. For instance: the grantor conveys by warranty deed, without benefit of title, the grantor later receives title, the grantor is prevented or estopped from asserting a better title against the grantee.

The covenant by estoppel is deemed to vest the after acquired title received by the grantor in the previous grantee: "His after acquired title is said to 'feed the estoppel' and by operation of law the title vest eo instante in the grantee..."

The doctrine has been used to prevent a grantor, who warranted good title, from asserting an easement across his previous conveyance, even when the title came from a third party. The courts have gone a step further and expanded the application of estoppel in North Carolina. The doctrine was used to prevent a grantor under a non-warranty deed from asserting a better title against a grantee when the deed on its face intended to convey the entire estate or fee. The court found that the effect of the deed was legally binding upon the grantor and those claiming under him, not a mere release of interest, and thus logic dictated estoppel. Where a conveyance is made by a quit claim deed,

(Continued on page 2)

In This Issue:

Warranties of Title...	1-3
NC Fun Facts	2
The Importance of Choosing a Qualified Intermediary Carefully	3
Claims Corner: But My Lender Said I Didn't Need a Survey!	4
Meet Our Title Attorneys	5
Investors Trust Company: Mitchell v. Brewer	5

Warranties of Title... (cont. from page 1)

when it is a mere release of interest, the estoppel will not operate; however, an expectation of title by the grantee might give rise to such a conclusion.

The doctrine of estoppel in North Carolina is effective between the grantor and grantee, but does not operate to estop third parties who are bona-fide purchasers for value. This necessary, and sometimes unfortunate, conclusion is the result of the application of the recording statute, the Conner Act, in conjunction with statutory recording and indexing requirements.

> "This necessary... conclusion is the result of application of the recording statute..."

The North Carolina Supreme Court has held on numerous occasions that prospective purchasers must be able to rely on the public records. The courts have reasonably limited the duty to search only to the chain of title of the subject property, and registration outside the chain of title has the same effect as no registration. The policy set forth by these decisions is that prospective purchasers and lien creditors must be able to rely on the public records. Simply put, allowing the doctrine of estoppel to operate as against the interest of third party purchasers for value would require all prospective purchasers to search outside the chain of title, and, as a result, change the nature and intent of the Conner Act.

> "...prospective purchasers and lien creditors must be able to rely on the public records."

Although estoppel is effective between the grantor and grantee in a warranty deed, or between the mortgagor and mortgagee, it will not operate to defeat lien creditors, judgment holders, deeds of trust, or bona-fide purchasers for value who have properly recorded their conveyance or lien. Practitioners should be careful when recording documents so that a hasty run to get documents on record does not inadvertently defeat the intent of the parties when documents are recorded out of order, exposing the lender to intervening liens.

The North Carolina Legislature, in 1969, made after acquired property clauses in deeds of trusts and mortgages ineffective as to lien creditors and purchasers, unless the instrument is re-registered, or registered after the additional property is acquired by the purchaser.

The legislature's intent to uphold the race requirement even in situations where the intent of the document was to secure all property and all property acquired thereafter, is dispositive and important to keep in mind. The courts have yet to hold that a deed of trust intending to convey presently

(Continued on page 3)

NC FUN FACTS

Marine Corps Air Station Cherry Point or **MCAS Cherry Point** is a United States Marine Corps airfield located in Havelock, North Carolina, USA, in the eastern part of the state and is the largest air base in the Marine Corps. It was built in 1941, was commissioned in 1942, and is currently home to the 2nd Marine Aircraft Wing. Congress authorized Marine Corps Air Station Cherry Point on July 9, 1941, with an initial appropriation of $14,990,000 for construction and clearing of an 8,000 acre (32 km^2) tract of swamps, farms, and timberland. Actual clearing of the site began on August 6, 1941, with extensive drainage and malaria control work. Construction began in November just 17 days before the attack on Pearl Harbor.

THE NC CONNECTION
AN INVESTORS TITLE COMPANY PUBLICATION

The Importance of Choosing a Qualified Intermediary Carefully

by Anna Gregory Wagoner, Title and Regulatory Attorney/Exchange Counsel
awagoner@invtitle.com

The recent federal indictment of a North Carolina man who provided qualified intermediary services is yet another reminder of the importance of choosing a qualified intermediary carefully. This individual was indicted for fraud, for a Ponzi scheme involving both his asset management company and his 1031 exchange services.

Unfortunately, this type of dishonest dealings with 1031 funds is not new. When one person owns the qualified intermediary company, and has all the control over the money being held, a disaster is waiting to happen.

This indictment is another illustration of the imprudence of having a sole practitioner CPA or attorney serve as qualified intermediary. An institutional qualified intermediary can provide safeguards that an individual qualified intermediary cannot; such as a carefully constructed disbursement control system, with multiple parties necessary to approve any disbursement; external and internal audits; daily and monthly reconciliations; segregation of client funds from operating funds; and the option to use a qualified trust as an additional safeguard, among others.

Investors Title Exchange Corporation has implemented all of the safeguards listed above and is available to assist you with your 1031 exchange transaction.

Investors Title Exchange Corporation
INNOVATIVE BY INSTINCT
SECURITY
EXPERTISE
SERVICE
www.1031itec.com

Warranties of Title... (cont. from page 2)

held property will operate to secure after acquired title against third party purchasers or lien creditors when the instrument is not re-recorded in the chain of title prior to the third party purchaser or lien creditor acquiring an interest.

Recording errors can become major problems. Even though estoppel is an equitable doctrine, the courts sparingly apply it, even when the party recording his deed or deed of trust has actual notice of the previous conveyance. In one case, a third party purchase money deed of trust was recorded before the owner/grantor became vested with title. A construction loan was placed on record after the deed with knowledge that third party purchase money loan was on record, but not in the chain of title. The court refused to apply estoppel in favor of the third party purchase money deed of trust. The court held that " . . . due recordation in the chain of title must remain the only effective means of protecting title."

The legislative preference for race over warranty makes the practitioner's burden much easier when this mandate for due recordation in the chain of title is understood. Modern and easily accessible records allow for an effective search of title to real property, making promises easier to keep and lessening the need for estoppel. The doctrine of estoppel will continue to protect purchasers from the grantor, but will not protect purchasers who do not make judicious use of North Carolina's recording statute.

But My Lender Said I Didn't Need a Survey!

By Carol Hayden, Claims Counsel

Why have lenders been afforded survey coverage without a survey while owners typically need a new or recent survey to obtain survey coverage? Most title insurers will give survey coverage to lenders, without a current survey, as long as there is evidence that the property had been surveyed by a Registered Land Surveyor at any time in the chain of title. This practice developed due to practical and business risk considerations, as well as lenders' widespread requests for waiver of the survey requirement. When this industry practice developed about a decade ago, a lender's interest in the collateral might have typically been 80-90% of the value of the property, and property prices were expected to rise. From an insurance risk perspective, it was less likely that a resulting matter affecting title would cause a loss under the lender's policy. The lender's claim would be ripe only when they suffered a loss upon acquiring the property in foreclosure, a less common occurrence previously than it is today. For example, if a deed overlap is present that would have been shown on an accurate survey, it might reduce the value of a property from $200,000 to $190,000. If the loan coverage was $180,000, the lender will not suffer a loss due to the title defect, resulting in no claim payment. The collateral was still worth more than the outstanding indebtedness and policy coverage, so there was no resulting loss to the lender. In today's economy, with property values declining and high foreclosure rates, title insurance companies are frequently covering lenders' losses they might not have expected to cover in the past. Let's say that today the same property's value has declined from $200,000 to $170,000, the homeowner has walked away from an upside-down loan, and the lender forecloses. The same deed overlap has now been discovered, reducing the property value to $160,000. The current loan indebtedness is $178,000, so the $10,000 diminution in value may be covered under the lender's policy.

Owners, on the other hand, have not been offered survey coverage without a survey. Typically, a title defect that would have been shown on an accurate survey would cause a loss to an owner where it might not cause a loss on a lender's policy. Many owners are very surprised when their claim is denied due to a survey exception in their title insurance policy. Their typical response is, "But, my lender said I didn't need a survey!", which actually translates that the lender did not *require* the owners to get a survey in order to close the loan. More troubling is the response, "But, my attorney said I didn't need a survey!" If an owner chooses not to purchase a survey, they should always be apprised of the risk they are taking.

Owners' title insurance claims have been denied, due to the policy survey exception, in the following instances when an accurate survey would have shown the defect:

- The land does not contain as many acres as purported
- Deed overlaps and resulting boundary disputes
- Rights of others to use roads or visit cemeteries on the subject property
- Encroachments of improvements located on the insured property onto neighboring property or onto easements
- Encroachments of improvements located on neighboring property onto the insured property
- Setback violations
- Visible unrecorded easements, such as utility lines crossing the property
- Title to filled in land, being claimed back by the State

Although the title insurance policy would have taken exception to these specific matters disclosed on a survey, the purchaser would clearly have had the advantage of knowing exactly what they were buying. The purchaser might have required the seller to resolve these matters, either monetarily, or curatively, prior to purchase, had the purchaser been aware of the defects. On the other hand, if the surveyor made an error and one of these matters is later discovered, by virtue of having survey coverage, an owner may be covered. The age-old saying, *"Caveat emptor"* still applies today. Make sure your client knows the risks and understands the policy exception, if they choose not to get a survey.

MEET OUR TITLE ATTORNEYS

David A. Bennington

Senior Vice President—Senior Title Attorney
daben@invtitle.com

David was born in Salem, Ohio and is a graduate of Culver Military Academy. He attended the University of North Carolina at Chapel Hill as a Morehead Scholar where he received a Bachelor of Arts in English with honors and was a member of Phi Beta Kappa. After a tour of duty as an officer in the U.S. Navy, David returned to UNC and earned his Juris Doctor in 1978. As a partner in a Hendersonville, North Carolina law firm, David focused on real estate and probate matters. He joined Investors Title Insurance Company in 1986. David is the author of supplements to *North Carolina Real Estate Title Searches* by Lilona and Gregory Schiro, and has been a seminar speaker on real property matters for Wake Forest University, The Mortgage Bankers Association of the Carolinas, and the North Carolina Paralegal Association. He is a past president of the North Carolina Land Title Association and a board-certified specialist in Real Property Law (residential transactions).

Investors Trust Company

Experience, Personal Service, Performance.

Mitchell v. Brewer

In a case that even the court describes as representing the principal of a "'cobbler's children [having] no shoes,'" the North Carolina Court of Appeals has ruled that a law firm that is dissolving may still file suit against other members of the firm. The case developed when a dispute arose at a partnership meeting in June 2005 about how to divide firm profits. The meeting concluded when a member of the firm, Glenn Adams, announced, "'I'm out of here…out of the firm.'" Several of the other attorneys in the firm followed Adams, and extensive litigation addressing various legal issues ensued, all of which, the appellate court observed, "stand or fall based [on]….whether this is a case of dissolution or withdrawal." As provided by state law, the Chief Justice of the North Carolina Supreme Court certified the litigation as a complex business case, and assigned it to the business court. The many issues were even more complicated because, even though the firm was organized as a professional limited liability company (PLLC), it had no operating agreement and, at different times, "seem[ed] to treat their business as a partnership and at other times as a PLLC…." The business court issued its opinion in March 2009, when it both granted and denied a number of partial summary judgments to each party, and then certified the case for appeal under Rule 54(b). In a 38-page decision that addressed matters ranging from which party had standing to whether the failure to verify a complaint was a jurisdictional issue, the appellate court both affirmed and reversed a number of the business court's decisions. It then ordered the case remanded to that court for additional proceedings on allegations of, *inter alia*, breaching fiduciary duties, conversion, unjust enrichment and derivative claims.

--*Mitchell v. Brewer,* No. COA09-1020, N.C. Ct. App. 2/1/11

The above article is for information purposes only and does not constitute legal advice.

- Personal service and individual attention delivered the old fashioned way.
- Customized portfolios constructed with individually managed stocks and bonds, for agency accounts, IRAs, and trusts.
- Over 200 years of combined experience from trusted investment and trust professionals who will work with you and your clients.

For more information, contact Ben Foreman at 877.327.9110 or bforeman@invtrust.com

www.invtrust.com

© 2011 Investors Title Company. All Rights Reserved.