Real Property

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Significant Changes in North Carolina 2011 Real Property Law

By James E. Creekman

NOTE: All of the attachments referenced in the following article are available in Word format at the following website: http://realproperty.ncbar.org/media/17498609/2011_Mortgage_Modernization_Act_Forms.pdf

During its 2011 Regular Session, the North Carolina General Assembly enacted four session laws that will have a significant impact on real estate practitioners, title insurance companies, and lenders that make loans secured by real property located in North Carolina:

Session Law 2011-246 (House Bill 312) – Entitled "An act amending the methods for recording satisfaction of a security instrument with the Register of Deeds, clarifying the requirements for electronically registering plats with the Register of Deeds, and amending restrictions on access to military discharge documents recorded with the Register of Deeds."

Session Law 2011-296 (House Bill 384) – Entitled "An act to simplify the fees charged for registering instruments with a Register of Deeds in this state and to modify the instrument page requirements."

Session Law 2011-351 (Senate Bill 519) – Entitled "An act to allow that a contract to convey real estate may be registered by registering a memorandum of contract and to require that deeds and deeds of trust prepared in other states and presented for registration to the Register of Deeds of any county in this state shall bear an entry showing the name of either the person or law firm who drafted the instrument."

Session Law 2011-312 (Senate Bill 679) – Entitled "An act to modernize and enact certain provisions regarding deeds of trust, including releases, short sales, future advance provision terminations and satisfactions, terminations and satisfactions for equity line liens, release of ancillary documents, eliminating trustee of deed of trust as necessary party for certain transactions and litigation, and indexing of subsequent instruments relating thereto."

Unless otherwise indicated, all of the changes described in this article will become effective Oct. 1, 2011. References in this article to the "existing" or "current" law means the law as it existed before Oct. 1, 2011.

This article highlights only those changes that will have a practical impact on real property practitioners and lenders.

RECORDING FEES

(Session Law 2011-296)

Attachment 1 to this article is a chart of the recording fees for real-estate related documents that will become effective Oct. 1, 2011.

G.S. 161-10 and G.S. 161-11.6 list the various fees charged by a Register of Deeds to record documents. Beginning October 1, 2011, the fees for recording real estate-related documents will be as follows:

1. Deeds of trust, mortgages, and cancellation of deeds of trust and mortgages.

   a. The basic fee for recording a mortgage or deed of trust will be $56 for the first 15 pages, plus $4 for each additional page or fraction thereof.

   b. The Register of Deeds may charge $10 for each additional instrument contained in a deed of trust or mortgage. A deed of trust or mortgage contains an additional instrument if the additional instrument (i) has a different legal consequence or intent, (ii) is separately executed and acknowledged, and (iii) could be recorded alone.

   c. As is currently the law, the Register of Deeds may not charge a fee for recording a record of satisfaction or other instrument that cancels a deed of trust or mort-

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gage.

2. Plats. The fee for recording a plat is unchanged – $21 per sheet or page.

3. Right-of-way plans. The fee for recording a right-of-way plan is unchanged – $21 for the first page and $5 for each additional page.

4. All other instruments affecting title to real property.

a. The basic fee for recording other instruments affecting title to real property will be $26 for the first 15 pages, plus $4 for each additional page or fraction thereof.

b. When a document presented for registration consists of multiple instruments, the Register of Deeds may charge an additional $10 for each additional instrument. A document contains an additional instrument if the additional instrument (i) has a different legal consequence or intent, (ii) is separately executed and acknowledged, and (iii) could be recorded alone.

c. G.S. 161-14.1(a)(3) defines a "subsequent instrument" as "[a]ny instrument presented for registration that indicates in its title or within the first two pages of its text that it is intended or purports to modify, amend, supplement, assign, satisfy, terminate, revoke, or cancel a pre viously registered instrument." When a subsequent instrument presented for registration refers to more than one original instrument, the Register of Deeds may charge an additional $25 for each additional reference.

5. Nonstandard documents. In addition to all other applicable fees, the Register of Deeds may charge an additional $25 to record any document that does not comply with the recording standards set forth in G.S. 161-14(b).

6. UCC financing statements. The fees for filing a UCC financing statement in the office of the Register of Deeds are unchanged:

a. $38 if the record being filed is written and consists of one or two pages.

b. $45 if the record being filed is written and consists of more than two pages, plus $2 for each page in excess of 10 pages.

c. $30 if the record is filed electronically.

Notes

• The current $2 add-on probate fee for the verification of proofs and acknowledgments authorized by G.S. 161-10(a)(16) is eliminated.

• In addition to all other recording fees, G.S. 161-11.6 currently requires a Register of Deeds to charge an additional $5 fee for the "archival of records" when a deed is recorded. The authority of the Register of Deeds to charge this additional $5 fee is suspended.

The changes in the registration fees represent a two-year experiment – the new fee structure will expire July 1, 2013. Unless the General Assembly acts in the inter-

im, the fees will revert to the pre-Oct. 1, 2011 fee structure. In the interim, the Revenue Laws Study Committee will review the effect of the changes to determine whether they have simplified the collection and remittance of fees by the Registers of Deeds. The committee has been tasked with reporting its findings to the General Assembly and recommending whether the temporary fee structure should revert on July 1, 2013, to the pre-Oct. 1, 2011 fee structure.

Format Requirements for Registration Of Instruments

(Session Law 2011-296 and Session Law 2011-351)

Effective Oct. 1, 2011, the margin and font size requirements that must be satisfied to register an instrument with the Register of Deeds are being relaxed slightly. Otherwise, the format requirements are unchanged.

1. G.S. 161-14(b) outlines the basic format requirements for all paper documents presented for registration (except UCC financing statements conforming to the requirements of G.S. 25-9-521). To be accepted by the Register of Deeds for recording, a paper instrument must satisfy the following requirements:

a. Be 8½ inches by 11 inches, or 8 ½ inches by 14 inches.

b. Have a blank margin of 3 inches at the top of the first page and blank margins of at least 0.25 inches (the current requirement is 0.5 inches) on the remaining sides of the first page and on all sides of subsequent pages.

c. Be typed or printed in black on white paper in a legible font. A font size no smaller than 9-points (the current requirement is 10-points) is considered legible. Blanks in an instrument may be completed in pen, and corrections to an instrument may be made in pen.

d. Have text typed or printed on one side of a page only.

e. State the type of instrument at the top of the first page.

If an instrument does not satisfy these requirements, the Register of Deeds may register the instrument after collecting a $25 fee for nonstandard documents in addition to all other applicable recording fees. However, if an instrument fails to meet the requirements because it contains print in a font size smaller than 9-points (the current requirement is 10-points), the Register of Deeds may register the instrument without collecting the fee for nonstandard instruments if, in the discretion of the Register of Deeds, the instrument is legible.

2. G.S. 47-17.1 requires that the first page of every deed or deed of trust state the name of either the person or law firm who drafted the instrument. Under the law as it previously existed, there was an exception for instruments prepared outside of North Carolina. That exception was eliminated by Session Law 2011-351 effective June 27, 2011. The first page of every deed and deed of trust (including those prepared outside of North Carolina) must now bear an entry showing the name of either the person or law firm who drafted the instrument.

3. With respect to mortgage and deed of trust satisfactions, G.S. 45-37(f) requires that an individual's signature be followed by the printed, stamped, or typed name of the individual signing the document so as to be clearly legible. The General Assembly made no change in this requirement.

Memoranda Filings

(Session Law 2011-351)

Article 8 of Chapter 47 of the General Statutes currently permits the filing of a memorandum of lease (G.S. 47-118) and a memorandum for an option to purchase real estate (G.S. 47-119). Session Law 211-351 added a new section, G.S. 47-119.1, that permits the filing of a "memorandum for contract to purchase real estate." The revisions to Article 8 of Chapter 47 became effective June 27, 2011.

Session Law 211-351 also amended G.S. 47-120, the statute that describes the legal effect of a recorded memorandum. When "executed, acknowledged, delivered and registered as required by law," a memorandum of a lease, an option to purchase real estate, or a contract to convey real estate "shall be as good and efficient notice, and have the same force and effect as if the written lease, option to purchase real estate, or contract to convey had been registered in its entirety." With the exception of adding the contract to convey real estate as an additional type of memorandum that may be recorded, this represents no change to existing law. However, in adding this third type of memorandum to the list, the General Assembly added an "automatic expiration" provision that applies only to a contract to convey real estate that is the subject of a recorded memorandum. Reduced to basics, a memorandum of a contract to convey real estate, whether recorded before or after June 27, 2011, will no longer be an impediment on the title to the real property described in the memorandum after the expiration of 60 days from whichever of the following events first occurs:

1. The closing date stated in the memorandum, or any recorded extension or renewal of the memorandum, that is signed and duly acknowledged.

2. The date when the conditions of the contract to convey were required to have been performed by the purchaser and seller according to the terms of the recorded memorandum, or any recorded extension or renewal of the memorandum, that is signed and duly acknowledged.

The Trustee in a Deed of Trust

(Session Law 2011-312)

Session Law 2011-312 has two sections that deal specifically with the trustee in a deed of trust.

1. The addition of a new subsection (c) to G.S. 45-10 resolves the longstanding question as to whether a deed of trust is a valid deed of trust (as opposed to a mortgage) if the trustee named in a deed of trust is also the beneficiary (or secured party) named in that deed of trust. According to G.S. 45-10(c), if the trustee named in a deed of trust is also the beneficiary named in the deed of trust, the instrument is deemed to be a deed of trust, and any substitute trustee named in the ordinary manner permitted under G.S. 45-10(a) succeeds to all of the rights, titles, authority, and duties of the trustee under the terms of the deed of trust.

Note: In 2009, the General Assembly resolved a related question – that is, whether an instrument that appears on its face to be intended to be a deed of trust is a valid deed of trust (as opposed to a mortgage) if no trustee is named in the instrument – i.e., the name of the trustee is omitted. G.S. 45-10(b) (which became effective June 26, 2009) provides that such an instrument is deemed to be a deed of trust and that the grantors who signed the deed of trust are deemed to be the "constructive trustees of record" for the secured party. The authority of the constructive trustees is quite limited, and the secured party is authorized at any time to name a substitute trustee who is not subject to the limitations applicable to the constructive trustees.

2. The other change has much broader implications. Effective October 1, 2011, the General Assembly has added a new section to the General Statutes, G.S. 45-45.3, which significantly reduces the role and responsibility of the trustee named in a deed of trust.

A little historical background is in order. Because the trustee in a deed of trust holds the "legal" (as opposed to the "equitable") title to the real property described in a deed of trust, real estate practitioners have always viewed the trustee as a necessary party to virtually any matter involving the property described in the deed of trust, including, for example, deeds of release, deed of trust modification agreements, and any litigation or proceeding involving the real property described in the deed of trust. In recent years, the role and responsibility of the trustee in a deed of trust has eroded somewhat. For example, G.S. 39-6.6 provides that the trustee of a deed of trust is not a necessary party to the subordination agreement unless the deed of trust provides otherwise. Similarly, although the trustee of a deed of trust may effect the cancellation of a deed of trust by recording a trustee's satisfaction pursuant to G.S. 45-36.20, a deed of trust may be cancelled of record by other means without the knowledge, joinder, or consent of the trustee – for example, by the secured creditor filing a document of satisfaction pursuant to G.S. 45-36.10.

New G.S. 45-45.3 dramatically changes these dynamics in the following respects:

a. Unless the deed of trust provides otherwise, any of the following may be done without the knowledge, consent, or joinder of the trustee:

(1) Pursuant to G.S. 45-36.23, an obligation may be declared by the owner and holder of the obligation to be no longer secured by the deed of trust. G.S. 45-36.23 is a new provision that is discussed in greater detail below.

(2) Property may be released from the lien of a deed of trust by the secured creditor. This is a new concept in North Carolina and obviates the need for a deed of release signed by both the secured creditor and the trustee.

(3) The lien of a deed of trust may be released or subordinated by the secured creditor. As to subordinations, this is a restatement of existing law as codified in G.S. 39-6.6(b).

(4) The terms of a deed of trust may be modified by the secured creditor and the then record owner of the property encumbered by the lien of a deed of trust. This is a dramatic change from current practice and warrants restating: Beginning Oct. 1, 2011, an instrument that modifies the terms of an existing deed of trust does not need to be signed by the trustee.

(5) The deed of trust may be satisfied of record by the secured party. This provision is a restatement of existing law as codified in G.S. 45-36.10.

b. Except in matters relating to the foreclosure of a deed of trust or the exercise of a power of sale under the terms of a deed of trust, the trustee named in a deed of trust is neither a necessary nor a proper party to a civil action or proceeding involving (i) title to the real property encumbered by the lien of the deed of trust or (ii) the priority of the lien of the deed of trust. By way of example, G.S. 45-45.3 provides that the trustee is neither a necessary nor a proper party to civil actions or proceedings relating to: (i) condemnation; (ii) bankruptcy; (iii) the establishment or correction of title to real property (including, for example, actions to quiet title, reform land records, or resolve boundary line disputes); (iv) fraudulent conveyances; (v) the creation or enforcement of an attachment or judgment lien; (vi) the foreclosure of a lien other than the lien of the deed of trust in question, regardless of whether the lien is superior or subordinate to the lien of the deed of trust (including, but not limited to, the foreclosure of mortgages, other deeds of trust, tax liens, and assessment liens); (vii) the establishment, per fection or enforcement of a mechanic's or materialman's lien; (viii) the creation or enforcement of a constructive trust, resulting trust, or equitable lien relating to the property; (ix) the partition of the property; (x) the interpretation or enforceability of a will, trust, or estate; (xi) a subrogation claim or other equitable claim or defense involving the priority or enforceability of a deed of trust; and (xii) determination or enforcement of rights and obligations involving

easements or restrictive covenants.

The bottom line is this – from a practical standpoint, beginning Oct. 1, 2011, the trustee named in a deed of trust should not be named as a party in any proceeding other than one involving the foreclosure or enforcement of the deed of trust itself.

c. G.S. 45-45.3(d) describes what happens when a trustee is improperly joined as a party to an action or proceeding when the new statute provides that the trustee is neither a necessary nor a proper party to that action or proceeding. If a motion to dismiss the trustee from the proceeding is filed by any party to the proceeding, the trustee must be dismissed. Regardless of whether the trustee makes an appearance in the proceeding, no entry of default or default judgment may be entered against the trustee. If the trustee makes an appearance in the proceeding, each person who improperly joined the trustee as a party is jointly and severally liable to the trustee for all of the expenses and costs incurred by the trustee in the defense of the proceeding or in obtaining the trustee's dismissal from the proceeding, including reasonable attorneys' fees actually incurred by the trustee.

d. To address the risk of unintended consequences and in an attempt to maintain North Carolina as a "title theory" state as opposed to a "lien theory" state, G.S. 45-45.3(e) provides that, except as expressly provided in G.S. 45-45.3, the new statute is "not in derogation of case law and statutory provisions that vest legal title to property conveyed by a deed of trust in the trustee named therein."

Practice Point: Recognizing that trustees named in deeds of trust will continue to be named as parties to lawsuits until litigators become familiar with the provisions of the new statute, trustees should prepare professional and polite letters that can be sent to litigants advising them of the provisions of G.S. 45-45.3 and requesting the voluntary dismissal of the trustee from the litigation.

Attachment 2 to this article is a template for a letter that can be used for this purpose.

Releases and Cancellations of Deeds of Trust

(Session Law 2011-246 and Session Law 2011-312)

Article 4 of Chapter 45 of the General Statutes is entitled "Satisfaction." Significantly amended in 2005 to incorporate many of the provisions of the Uniform Mortgage Satisfaction Act, Article 4 provides the mechanics for the cancellation of deeds of trust from public record. Session Laws 2011-246 and 2011-312 significantly amend the satisfaction article to address issues that have arisen since 2005.

1. Methods to Cancel a Deed of Trust – G.S. 45-37(a) and G.S. 45-37.2(b). One of the most commonly used methods for cancelling a deed of trust from public record has long been to present to the Register of Deeds the original of the note and deed of trust marked "Paid in Full and Satisfied." The deed of trust is then cancelled as a matter of public record by recording a "record of satisfaction." Under current law as provided in G.S. 45-37.2(b), this requirement is satisfied when either (i) all or a portion (typically only the first page) of the original deed of trust containing the endorsement of payment and satisfaction is rerecorded, or (ii) the Register of Deeds prepares, signs, and records a separate record of satisfaction form. Beginning Oct. 1, 2011, this method of cancellation will no longer be available – to cancel a deed of trust, it will be necessary to record (i) a satisfaction document pursuant to G.S. 45-36.10, (ii) an affidavit of satisfaction pursuant to G.S. 45-36.16, or (iii) a trustee's satisfaction pursuant to G.S. 45-36.20. In addition, Registers of Deeds will no longer be required to make marginal notations on recorded documents.

2. Document of Rescission – G.S. 45-36.6. As currently written, G.S. 45-36.6 provides a mechanism to reinstate a deed of trust that was cancelled in error. Effective Oct. 1, 2011, G.S. 45-36.6 is rewritten to provide a mechanism to rescind (i) the erroneous satisfaction of a deed of trust, (ii) a document recorded in error that releases property from the lien of a deed of trust, or (iii) a document recorded in error that declares that a specific obligation is no longer secured by a deed of trust. The amended statute also provides two "document of rescission" forms that can be used by real estate practitioners and lenders for these purposes.

Attachment 3 to this article is a generic "Document of Rescission" that may be used to rescind a release that was recorded in error.

Attachment 4 to this article is a generic "Document of Rescission" that may be used to rescind the erroneous satisfaction of a deed of trust.

Although the recording of an appropriate document of rescission will reinstate a deed of trust cancelled in error or rescind the effect of an erroneously recorded release, the document of rescission will have no legal effect on anyone who records an interest in the real property during the period of time between the time the erroneous action was taken and the date the document of rescission was recorded. Thus, for example, a reinstated deed of trust will not have priority over a deed of trust that was recorded during the "gap" period.

Practice Point: A word of caution is in order. If the promissory note secured by the deed of trust and/or the deed of trust itself have been marked "Paid in Full and Satisfied" and sent to the borrower, it may be too late for the lender to reverse the erroneous cancellation of the deed of trust by merely filing a document of rescission, and filing a document of rescission may invite litigation. A lender may more safely rely on G.S. 45-36.6 if the original of the promissory note and deed of trust are in the lender's possession and the borrower acknowledges in writing that the deed of trust was erroneously cancelled or the release instrument erroneously recorded.

3. Partial Releases – G.S. 45-36.22. The preferred method of releasing some (but not all) property from the lien of a North Carolina deed of trust has historically been a deed of release signed by both the secured creditor and the trustee named in the deed of trust. Effective Oct. 1, 2011, G.S. 45-36.22 creates an alternative mechanism for the

release of property from a deed of trust – a "partial release." Lenders may prefer using a partial release because it does not require the signature of the trustee named in the deed of trust.

Functioning in much the same way as a deed of release, a partial release releases the property specifically described in the partial release from the lien of the deed of trust. The deed of trust otherwise remains in full force and effect, and the remainder of the property described in and encumbered by the deed of trust remains subject to its lien. A partial release will be effective to release property from the lien of a deed of trust if it is signed by (i) the secured creditor, (ii) the trustee or substitute trustee, or (iii) both the secured creditor and the trustee or substitute trustee. While no particular phrasing is required for a partial release, the statute provides a form which, if used, is sufficient to satisfy the requirements of G.S. 45-36.22.

Attachment 5 to this article is a generic "Partial Release" that should satisfy the requirements of G.S. 45-36.22.

4. Obligation Release – G.S. 45-36.23. G.S. 45-36.23 is a new statute that permits a lender, without the knowledge, consent, or joinder of the trustee, to declare that certain specific obligations are no longer secured by a deed of trust. While no particular phrasing is required for an obligation release, the statute provides a form which, if used, is sufficient to satisfy the requirements of G.S. 45-36.23.

Attachment 6 to this article is a generic "Obligation Release" that should satisfy the requirements of G.S. 45-36.23.

5. "Life of Lien" Statute – G.S. 45-36.24. G.S. 45-37(b) is North Carolina's existing "life of lien" statute. It provides that the lien of a deed of trust will automatically expire 15 years from the last to occur of (i) the date when the conditions of the deed of trust were required by its terms to have been performed, or (ii) the maturity date of the last installment of debt or interest secured by the deed of trust. Thus, if the maturity date of the obligation secured by a deed of trust is not stated on (or cannot be conclusively determined from) the text of the deed of trust, the public record does not provide a means of determining the expiration of the lien without investigating documents that are not a matter of public record, often unavailable many years later.

The 2011 General Assembly enacted a new life of lien statute, G.S. 45-36.24, which becomes effective Oct. 1, 2011. The new statute provides certainty as to the date the lien of a deed of trust will automatically expire in order to remove old liens that are a cloud on title and to "clean up" the public record. The new statute does not have any impact on the statute of limitations applicable to a secured obligation or on G.S. 45-21.12, which bars the foreclosure of a deed of trust when recovery on the secured obligation is barred by the statute of limitations applicable to that obligation. In short, the statute does not prolong the period of time within which a deed of trust may be foreclosed.

As contemplated by G.S. 45-36.24:

a. The life of the lien of a deed of trust is determined by whether the maturity date of the secured obligation is stated in the deed of trust. If the maturity date of the secured obligation is stated in the deed of trust, the lien of the deed of trust will automatically expire 15 years from that maturity date. If the maturity date of the secured obligation is *not* stated in the deed of trust, the lien of the deed of trust will automatically expire 35 years from the date the deed of trust was recorded. However, a special rule applies to deeds of trust recorded before Oct. 1, 2011, the effective date of the act – the old rule stated in G.S. 45-37(b) is grandfathered in as an additional factor to prevent the life of the lien of a deed of trust from being inadvertently extended by the "bright light" test of the new 15/35 rule – in other words, the lien of an existing deed of trust will automatically expire under the old test or the new test, whichever causes the lien to expire first.

Thirty-five years was chosen as the magic number for the life of the lien of a deed of trust for a very practical reason. It provides a five-year "cushion" following the normal maturity of a 30-year home loan without requiring the filing of any subsequent instruments. However, it is important to remember that the proposed 35-year rule will apply only if the maturity date of the secured obligation is not stated in the deed of trust. If the maturity date of the secured obligation is stated in the deed of trust, the lien will automatically expire 15 years from the stated date – the same rule now in effect under the law as currently written.

b. G.S. 45-36.24(c) permits the life of the lien of a deed of trust to be "fixed" and/or extended by the filing of either (i) a "lien maturity extension agreement" or (ii) a "notice of maturity date." The statute contemplates the possibility that multiple lien maturity extension agreements and/or notice of maturity date documents may be recorded with respect to a single deed of trust. However, regardless of which form is used to extend the life of the lien, the document must be recorded while the lien is still "live" in order to be effective. Filing a lien maturity extension agreement or notice of maturity date cannot revive a lien that has already expired.

(1) A "lien maturity extension agreement" extends the life of the lien to a specific date. A lien maturity extension agreement must be signed by both the secured creditor and the then owner of the property. The trustee named in a deed of trust does not have to be party to a lien maturity extension agreement. While no particular phrasing is required for a lien maturity extension agreement, the statute provides a form which, if used, is sufficient to satisfy the requirements of G.S. 45-36.24.

Attachment 7 to this article is a generic "Lien Maturity Extension Agreement" that should satisfy the requirements of G.S. 45-36.24(d).

(2) A "notice of maturity date" places on public record the maturity date of the secured obligation. A notice of maturity date may be signed by (i) the secured creditor

only, or (ii) the secured creditor and the then owner of the property. The trustee named in a deed of trust does not have to be party to a notice of maturity date.

(a) Unlike the lien maturity extension agreement, a notice of maturity date is effective when signed only by the secured creditor, even without the consent or joinder of the then owner of the property. However, if the notice is signed only by the secured creditor, the lien of the deed of trust will automatically expire 15 years after the maturity date stated in the notice or 50 years from the date the deed of trust was originally recorded, whichever first occurs. This limitation serves as a protection against the lender unilaterally converting a deed of trust to an "evergreen" deed of trust. While no particular phrasing is required for a notice of maturity date, the statute provides a form which, if signed only by the secured creditor, is sufficient to satisfy the requirements of G.S. 45-36.24.

Attachment 8 to this article is a "Notice of Maturity Date" to be signed only by the secured creditor that should satisfy the requirements of G.S. 45-36.24(e).

(b) If the notice of maturity date is signed by both the secured creditor and the then owner of the property, the lien of the deed of trust will automatically expire 15 years after the maturity date stated in the notice. Virtually any document that modifies, amends, or restates a deed of trust will constitute a notice of maturity date, provided it (i) identifies the deed of trust, the original parties to the deed of trust, and the recording information for the deed of trust, (ii) states the maturity date of the obligation secured by the deed of trust, and (iii) is duly signed and acknowledged by both the secured creditor and the then owner of the property. As a result, G.S. 45-36.24 does not provide a model form for a notice of maturity date to be signed by both the secured creditor and the then owner of the property.

Practice Point: A word of caution with respect to lien maturity extension agreements – if a lien maturity extension agreement is recorded that designates the maturity date of the secured obligation as the date the lien of the deed of trust will automatically expire, the lien of the deed of trust will "fall off" on the maturity date of the note and the lender will not be able to foreclose the deed of trust if the note has not been paid in full. For this reason, a prudent lender's counsel will probably recommend using a notice of maturity date to extend the life of the lien of a deed of trust that secures repayment of a promissory note because the lien will not automatically expire for some period of time after the note matures – there is a built-in cushion of time to permit appropriate collection efforts, including foreclosure. However, it may be appropriate to use a lien maturity extension agreement to extend the life of the lien of a deed of trust when the secured obligation has no specific maturity date – for example, when a deed of trust secures a guarantor's payment obligations under an unconditional continuing guaranty agreement.

c. The life of the lien of a deed of trust cannot be shortened without the consent of the secured creditor.

6. Automatic Release of Real Property from Ancillary Security Instruments – G.S. 45-42.3. In addition to recording a deed of trust on the real property, it is not uncommon for lenders to file a separate assignment of rents and/or a UCC financing statement covering fixtures on the real estate. When the deed of trust is cancelled or property is released from the lien of the deed of trust, cancellation of the related assignment of leases and/or termination of the related UCC financing statement is often overlooked.

New G.S. 45-42.3, entitled "Automatic Release of Real Property from Ancillary Security Instruments," is intended to address this situation. The statute defines an "ancillary security instrument" to include an assignment of leases, an assignment of rents, a financing statement covering fixtures that is filed in the Office of the Register of Deeds, and any other document or instrument that assigns, or creates a lien on, an interest in real property.

G.S. 45-42.3 provides for the automatic release of property from ancillary security instruments when the related deed of trust is cancelled or property is released from the lien of the deed of trust. The rule does not apply, however, if (i) the ancillary security instrument secures obligations other than, or in addition to, the obligation or obligations secured by the deed of trust, or (ii) any of the instruments indicate that the ancillary security instrument is unaffected by the cancellation of the related deed of trust or the release of property from the deed of trust.

Practice Point: Attorneys and lenders that want to avoid the automatic cancellation of ancillary security instruments (or the automatic release of property from ancillary security instruments) should consider including the following provision in their deeds of trust:

Ancillary Security Instruments. The satisfaction of this Deed of Trust of record shall not release the real property described in this Deed of Trust from the operation of any ancillary security instrument. A partial release or deed of release that releases real property from the lien of this Deed of Trust shall not release real property from the operation of any ancillary security instrument. For purposes of this provision, the term "ancillary security instrument" has the same meaning as is set forth in section 45-42.3 of the North Carolina General Statutes.

Attorneys certifying title to real property will need to be cautious in relying on G.S. 45-42.3 as a basis for opining that an ancillary security instrument was automatically cancelled when the related deed of trust was cancelled. Both the deed of trust and the ancillary security instrument must be carefully examined to ensure that (i) they secure exactly the same secured obligation and that neither secures any obligation or obligations not secured by the other, and (ii) that neither the deed of trust nor the ancillary security instrument contains language (such as that above) that serves to override G.S. 45-42.3 to keep the ancillary security instrument "live."

Payoff Statements and Short-Pay Statements

(Session Law 2011-312)

The adoption of G.S. 45-36.7 in 2005 introduced a mechanism for borrowers to obtain firm loan payoff statements for existing deeds of trust. While a payoff statement specifies the amount required to pay a loan secured by a deed of trust in full, there is currently no mechanism for a borrower to obtain a "short-pay" statement – that is, a statement identifying the sum necessary to obtain the release of all or a specific portion of the real property from the lien of a deed of trust without satisfying the secured obligation in full. A short-pay statement will typically be required by a settlement agent in anticipation of (i) a short sale of all of the property encumbered by the lien of a deed of trust (i.e., a sale of all of the property for a price less than the amount owed on the loan – a common situation in these troubled economic times), or (ii) the sale of a portion of the real property encumbered by the lien of the deed of trust under circumstances requiring the release of that property from the lien of the deed of trust (i.e., a partial release).

In addition to lacking a mechanism to obtain "short-pay" statements, the list of individuals authorized to obtain payoff statements under G.S. 45-36.7 has proven to be too restricted. These issues have been addressed in Session Law 2011-312. In anticipation of the changes that will become effective Oct. 1, 2011, lenders will need to develop new forms and procedures to request short-pay statements from other lenders and to respond to requests for payoff and short-pay statements from a significantly broader group of parties.

1. Short-Pay Statements. Effective Oct. 1, 2011, the scope of G.S. 45-36.7 is expanded to include short-pay statements in addition to payoff statements.

> a. The mechanism for processing a request for a short-pay statement is almost identical to the current statutory mechanism for processing a payoff statement request. However, the request for a short-pay statement must include a clear statement as to whether the request is for the short-pay amount required to release all of the real property described in the deed of trust or only a portion of the property. If the request is for the short-pay amount required to release only a portion of the property, the request must include the description of the specific real property to be released upon payment of the short-pay amount.
>
> b. Unless the short-pay statement expressly provides otherwise, all persons liable for payment or performance of the obligation secured by the deed of trust will remain liable for the secured obligation to the extent the short-pay amount is insufficient to satisfy the secured obligation in full. This warrants repeating: Unless the short-pay statement expressly states otherwise, the borrower remains liable for any deficiency owed on the secured obligation, even if the short sale results in the release of all of the property from the deed of trust. This is an important provision to remember in connection with a true short sale of the property.
>
> c. G.S. 45-36.6(h) requires a secured creditor to provide on request one payoff statement or one short-pay statement without charge during any six-month period. The secured creditor may charge a fee of $25 for each additional payoff statement and $100 for each additional short-pay statement requested during that six-month period.

It is worth noting that, unless the loan documents provide otherwise, a lender is not typically required to release all or any portion of the property described in a deed of trust unless and until the secured obligation and all other sums secured by the deed of trust have been paid and satisfied in full. Accordingly, unless the loan documents provide otherwise (for example, when the loan documents provide for the release of individual subdivided lots when they are sold and the designated release price is paid), a lender may elect to respond to a request for a short-pay statement by providing a payoff statement for the full amount owed and stating that the lender will not permit the release of all or any portion of the property from the lien of the deed of trust until the secured obligation is paid in full.

2. Who Can Obtain a Payoff or Short-Pay Statement? Under existing law, the only people authorized to obtain a payoff statement are (i) a person liable for payment or performance of the secured obligation (or an agent authorized by that person), or (ii) the landowner (or an agent authorized by the landowner). The narrow universe of "entitled persons" authorized to obtain a payoff statement has proven problematic for lenders, title insurance companies, and real estate practitioners. Beginning Oct. 1, 2011, G.S. 45-36.4 and G.S. 45-36.7 provide that each of the following (and the agents authorized by each of the following) is considered an "entitled person" authorized to request a payoff or short-pay statement from the secured creditor:

> a. A borrower – that is, a person primarily liable for payments or performance of the obligation secured by the real property described in the deed of trust.
>
> b. A landowner – that is, a person that, before foreclosure, has the right of redemption in the real property described in the deed of trust. The term "landowner" does not include a person that holds only a lien on the real property or the trustee under a deed of trust.
>
> c. A person who has contracted to purchase real property encumbered by an existing deed of trust.
>
> d. A person who has made or has committed to make a loan that is secured or is to be secured by real property encumbered by an existing deed of trust – for example, a lender that is financing the purchase of the property or refinancing an existing loan.
>
> e. A title insurance company authorized to issue title insurance policies in North Carolina that has insured or has committed to insure title to real property encumbered by the deed of trust.
>
> f. The foreclosing trustee or the high bidder in a foreclosure sale involving the real property encumbered by the deed of trust.

g. A person who is a "qualified lienholder" – that is, a person who holds or is the beneficiary of a security interest in or lien on real property encumbered by an existing deed of trust, but only if that person's security interest in or lien on the real property arises from a mortgage or deed of trust that is subordinate in priority to the lien of the existing deed of trust. The term "qualified lienholder" does not include the trustee under a deed of trust.

h. A person who is an attorney licensed to practice law in North Carolina or a bank, savings and loan association, savings bank, or credit union, but only when (i) the attorney, bank, savings and loan association, savings bank, or credit union is or will be responsible for the disbursement of funds in connection with the sale of, or a new loan secured by, property then encumbered by an existing deed of trust; and (ii) a requirement of the sale or new loan transaction is or will be that the property be conveyed or encumbered free and clear of the lien of the existing deed of trust.

In summary, the list of persons authorized to obtain a payoff or short-pay statement has been broadly expanded to include almost anyone who has a legitimate need to know the payoff or short-pay amount.

Practice Pointer: Beginning Oct. 1, 2011, the authority of an attorney licensed to practice law in North Carolina to request a payoff statement or a short-pay statement from a lender pursuant to G.S. 45-36.7 is greatly expanded. For example, a licensed attorney can request and obtain a payoff statement or a short-pay statement if the attorney:

- Is an agent authorized (hopefully in writing!) by an "entitled person" to request a payoff statement or a short-pay statement.

- Is the foreclosing trustee in a foreclosure sale involving real property encumbered by an existing deed of trust. This provision will permit the trustee foreclosing under a subordinate deed of trust to obtain payoff information regarding a superior deed of trust, thereby enabling bidders to calculate a "rational" bid.

- Will handle the closing and disbursement of funds in connection with the sale of, or a new loan secured by, property then encumbered by an existing deed of trust, but only if a requirement of the sale or new loan transaction is that the property be conveyed or encumbered free and clear of the lien of the existing deed of trust. This provision will permit the closing attorney to obtain a payoff statement or short-pay statement even if the attorney does not represent the person whose loan is to be paid off – for example, when the closing attorney represents the buyer and not the seller in a sale transaction.

Articles 7 And 9 Of Chapter 45 – A Primer On Future Advance Deeds Of Trust And Equity Lines Of Credit

Background.

A fundamental principle of real property law in North Carolina is that the lien priority of a deed of trust is determined by the date the deed of trust is recorded in the office of the Register of Deeds in the county where the real property is located. With only minor exceptions, North Carolina is considered a "race" state – that is, whoever wins the race to the courthouse to record his deed of trust first, wins. As a result, the rule can be easily described as "first in time, first in line."

This is a simple and straightforward legal principle to apply when all of the proceeds of the secured obligation are disbursed at the time the deed of trust that secures that obligation is recorded. What happens, however, when loan proceeds are disbursed well after the deed of trust is recorded – for example, when the loan proceeds in a construction loan are disbursed as construction progresses, or when a borrower obtains credit advances years later under a revolving line of credit? What happens if competing liens on the property arise between the date the deed of trust was recorded and loan proceeds are disbursed?

The North Carolina General Assembly has addressed these issues in Articles 7 and 9 of Chapter 45 of the General Statutes. Article 7 is entitled "Instruments to Secure Future Advances and Future Obligations." Article 9 is entitled "Instruments to Secure Equity Lines of Credit." A little historical background is necessary to understand why we have two articles dealing with the same basic issue.

Article 7 of Chapter 45 is the "old" future advance statute that has been in effect for over forty years – it was originally adopted in 1969 – and has been amended only slightly since that time. In contrast, Article 9 was not adopted until 1985, when home equity lines of credit first became popular. At that time, Article 7 was viewed as too cumbersome to be used in connection with home equity lines of credit, possibly because revolving lines of credit secured by deeds of trust on real property were relatively new in the marketplace and there was uncertainty as to whether Article 7 provided adequate protection for lenders.

In any event, we have inherited two separate articles that deal with the priority of deeds of trust that secure future advances. The underlying principle of each is the same – and that principle resolves the issues described above. Provided (i) the appropriate "magic language" appears in the deed of trust and (ii) the advances are made within the prescribed time periods, future advances secured by an Article 7 or Article 9 deed of trust will have priority for lien purposes that relates back to the date the deed of trust was recorded, thereby "trumping" intervening liens.

Although Article 7 and Article 9 have been largely homogenized in recent years, there are some important and notable differences between the two articles:

1. An Article 7 deed of trust can secure either an open-end (or revolving) line of credit or a closed-end line of credit (such as a construction loan). Article 9 deeds of trust can secure only a revolving line of credit – they should never be used to secure a closed-end line of credit.

2. To achieve the desired lien priority, Article 7 and Article 9 deeds of trust must include the appropriate "magic language":

a. For Article 7 deeds of trust, the deed of trust must recite

(i) that it "is given wholly or partly to secure future advances and/or future obligations," (ii) the maximum principal amount that may be secured by the deed of trust at any one time, and (iii) the period within which future advances may be made and future obligations may be incurred. This period may not extend more than thirty (30) years beyond the date of the deed of trust (or, if the deed of trust is not dated, the date the deed of trust is recorded).

b. For Article 9 deeds of trust, the deed of trust must (i) show on its face the maximum principal amount that may be secured at any one time, and (ii) show on its face that it secures an equity line of credit governed by the provisions of Article 9 of Chapter 45 of the North Carolina General Statutes.

3. An Article 7 deed of trust can secure both future advances and future obligations. While an Article 9 deed of trust can secure future advances, it cannot secure future obligations. What's the difference between a "future advance" and a "future obligation"? An "advance" is defined in Article 7 as a disbursement of funds or other action that increases the outstanding principal balance owing on an obligation for the payment of money. An "obligation" is not a defined term, but common sense suggests that the term includes a note or credit agreement – that is, a credit facility that gives rise to an advance. Thus, Article 7 may secure both existing obligations (i.e., notes that are in existence on the date the deed of trust is recorded) as well as future obligations (i.e., notes signed in the future). Correspondingly, future advances (i.e., the disbursement of loan proceeds that increases the outstanding principal amount owing on an obligation) may occur with respect to either existing obligations or, when incurred, future obligations.

Practice Point: Although an Article 7 deed of trust can be used to secure existing and/or future obligations, you should not attempt to use an Article 9 deed of trust to secure an obligation to be incurred in the future.

Amendments to Article 7:

Effective Oct. 1, 2011, Session Law 2011-312 makes the following clarifying amendments to Article 7:

1. G.S. 45-68 is amended to make it clear that obligations secured by a future advance deed of trust can be specifically or generally identified, described or referenced in the deed of trust, thereby facilitating "dragnet" or "spreader" clauses.

2. G.S. 45-70(a1) addresses the treatment of the outstanding balance of an obligation secured by a future advance deed of trust to the extent the balance owed exceeds the maximum principal amount that may be secured by the deed of trust at any one time. Under G.S. 45-69 as currently written, if the amount owed exceeds the maximum principal amount that may be secured by the deed of trust at any one time, the excess is not secured by the deed of trust. Amendments to G.S. 45-69 and new G.S. 45-70(a1) reverse this rule – unless the deed of trust provides otherwise, the excess is secured by the deed of trust, but not with a priority that relates back to the date the deed of trust was recorded.

3. G.S. 45-70(c) clarifies that (i) accrued interest and certain payments made, sums advanced, and expenses incurred by the lender to protect the collateral and the lender's lien position are secured by the deed of trust with a priority as of the date the deed of trust was recorded, and (ii) those sums are not included in the calculation of the principal amount that may be secured by the deed of trust at any one time.

Amendments to Article 9:

Effective Oct. 1, 2011, Session Law 2011-312 makes the following substantive changes to Article 9:

1. The definitions section, G.S. 45-81, has been significantly revised and expanded.

2. The prohibition against charging a prepayment penalty in connection with an equity line of credit has been moved from G.S. 45-81(c) to its own separate section, G.S. 45-82.4. It is important to remember that a very limited exception to the prepayment penalty prohibition appears in G.S. 24-9(c) – the provision in the usury statute that permits a lender to "term out" a portion of the outstanding principal balance owing on an equity line of credit at a fixed interest rate and to include a prepayment penalty provision that applies only to the prepayment of the amount "termed out."

3. G.S. 45-82 is amended to clarify that (i) accrued interest and certain payments made, sums advanced, and expenses incurred by the lender to protect the collateral and the lender's lien position are secured by the deed of trust with a priority as of the date the deed of trust was recorded, and (ii) that those sums are not included in the calculation of the principal amount that may be secured by the deed of trust at any one time.

4. The procedures stated in G.S. 45-82.1 for extending the period of time within which future advances can be made has been refined. The statute provides a revised form which, if used, is sufficient to satisfy the requirements of the statute.

Attachment 9 to this article is a "Certificate of Extension of Period for Advances under Equity Line of Credit" for use by a lender that should satisfy the requirements of G.S. 45-82.1.

5. Discussed in significantly greater detail below in this article, two new sections – G.S. 45-82.2 and G.S. 45-82.3 – facilitate the termination of equity lines of credit and the cancellation of related deeds of trust.

Cutting Off and Cancelling Equity Lines of Credit

(Session Law 2011-312)

Future advance deeds of trust have posed some of the most vexing problems encountered by real estate practitioners, title insurance companies, and lenders since home equity lines of credit became commonplace. These problems arise from the fundamental nature of

a revolving line of credit – the borrower can obtain credit advances as long as the credit line is open, and the outstanding balance will fluctuate as advances are obtained and repaid. Reducing the outstanding balance to zero does not automatically result in termination of the line of credit. As a result, when the balance is paid to zero, a lender does not know to terminate the line of credit and cancel the related deed of trust unless the lender is clearly instructed to do so. Two examples highlight the problems:

Example 1. Mr. and Mrs. Johnson contract to sell their home to Mr. and Mrs. Baker. The property is currently encumbered by a $350,000 home equity line of credit that has an outstanding balance of $100,000. An attorney, Mr. Smith, handles the closing of the sale transaction on behalf of the purchasers. Instead of obtaining a binding payoff statement as permitted under G.S. 45-36.7, Mr. Smith relies on an informal statement from the home equity lender as to the balance due on the home equity line of credit and the amount sufficient to pay it off. That statement is obtained five days before closing. Mr. Smith handles the closing of the sale transaction and wires funds to the home equity lender. The amount he wires is sufficient to pay off the home equity line of credit according to the informal payoff quote he received from the lender, but not the full balance then owing. Unbeknownst to the purchasers or Mr. Smith, Mr. and Mrs. Johnson obtained an additional advance on their home equity line of credit between the date Mr. Smith asked for the payoff quote and the date the sale was consummated. Wouldn't it have been helpful for Mr. Smith to have been able to "freeze" Mr. and Mrs. Johnson's home equity line of credit during that brief period of time in anticipation of the sale of their property?

Example 2. Mr. and Mrs. Rogers want to "term out" their existing $350,000 home equity line of credit. To that end, they are approved for a 30-year $350,000 conventional mortgage loan. The refinancing lender requires that the home equity line of credit be paid off and the related deed of trust cancelled, which will put the new refinancing deed of trust in first lien position. The closing attorney handles the refinancing transaction without incident and wires to the home equity lender an amount sufficient to reduce the outstanding balance in the home equity line of credit to zero. Unfortunately, neither the borrower nor the attorney provide clear and adequate instructions to the home equity lender to terminate the line of credit and cancel the deed of trust as contemplated by G.S. 45-36.9(a) and G.S. 45-81(c). As a result, although the outstanding balance of the home equity line of credit is reduced to zero, the line of credit is not terminated and the related deed of trust is not cancelled. Sometime thereafter, the borrowers realize that their home equity line of credit is still "live," and they again obtain credit advances on the line of credit. Because the deed of trust securing the home equity line of credit was never cancelled, it remains in a first lien position, superior to the deed of trust that secures the refinancing loan (and that was intended to be secured by a first lien on the property). This problem could have been avoided had there been an easy mechanism to terminate the existing home equity line of credit and effect the cancellation of the deed of trust that secured the home equity line of credit.

Session Law 2011-312 goes to great lengths to address these issues by providing pre-closing, closing, and post-closing mechanisms to freeze a line of credit and, when appropriate, compel the termination of the line of credit and cancellation of the related deed of trust when the loan balance is reduced to zero.

1. Amendment of G.S. 45-36.9(a). The first significant change involves an amendment to G.S. 45-36.9(a). As currently written, G.S. 45-36.9(a) requires a lender to cancel a deed of trust within 30 days after the lender receives "full payment or performance of the secured obligation." However, if the deed of trust secures a line of credit or future advances, the current law provides that a "secured obligation is fully performed only if, in addition to full payment, the secured creditor has received a notification requesting the creditor to terminate the line of credit or containing a statement sufficient to terminate the effectiveness of the provision for future advances" in the deed of trust. Effective Oct. 1, 2011, G.S. 45-36.9(a) is amended to read as follows:

> A secured creditor shall submit for recording a satisfaction of a security instrument within 30 days after the creditor receives full payment or performance of the secured obligation. If a security instrument secures a line of credit or future advances, the secured obligation is fully performed only if, in addition to full payment, the secured creditor has received (i) a notification requesting the creditor to terminate the line of credit, (ii) a credit suspension directive, or (iii) a notification containing a clear and unambiguous statement sufficient to terminate the effectiveness of the provision for future advances in the security instrument including, but not limited to, a request to terminate an equity line of credit given pursuant to G.S. 45 82.2 or a notice regarding future advances given pursuant to G.S.45 82.3.

G.S. 45-36.9(a) references three new documents – a "credit suspension directive," a "request to terminate an equity line of credit" given pursuant to G.S. 45-82.2, and a "notice regarding future advances" given pursuant to G.S. 45-82.3. These three new documents are discussed in detail below.

2. Credit Suspension Directive – G.S. 45-36.7A. A new section, G.S. 45-36.7A, introduces credit suspension directives. A credit suspension directive is defined in G.S. 45-36.4(1b) as a notice given to a secured lender pursuant to G.S. 45-36.7A directing the lender to suspend temporarily a borrower's right and ability to obtain additional credit advances in anticipation of the imminent sale of, or the imminent making of a new loan to be secured by, real property then encumbered by an existing deed of trust when the anticipated transaction will involve either the satisfaction of the existing deed of trust or the release of the real property from the lien of the existing deed of trust. In simpler terms, a credit suspension directive is really nothing more than a document that permits a line of credit to be "frozen" in anticipation of the imminent closing of a transaction which, by its terms, will require either the satisfaction of the existing deed of trust or the release of the property from the lien of the existing deed of trust.

As contemplated by G.S. 45-36.7A:

a. To be effective, a credit suspension directive must contain all of the following:

(1) The name and authority of the person giving the directive.

(2) Sufficient information to enable the lender to identify the secured obligation, the identity of the borrower, and the real property encumbered by the deed of trust.

(3) The specified payoff date, which may not be more than thirty (30) days after the notification is given.

(4) A clear and unambiguous directive to the lender to suspend the borrower's right and ability to obtain any additional credit advances through and including the payoff date.

b. A credit suspension directive may be given to the lender by the borrower (or any borrower if there is more than one), the legal representative of any borrower, or the attorney for any borrower. In addition (and more importantly), a credit suspension directive may be given by an attorney licensed to practice law in North Carolina or a bank, savings and loan association, savings bank, or credit union, but only if all of the following conditions are satisfied:

(1) The attorney or financial institution must be responsible for the disbursement of funds in connection with the sale of, or a new loan to be secured by, the real property then encumbered by the existing deed of trust – in other words, the attorney or financial institution must be the settlement agent for the anticipated sale or loan transaction involving the property secured by the existing deed of trust.

(2) A requirement of the sale or new loan transaction is that the property be conveyed or encumbered free and clear of the lien of the existing deed of trust.

(3) The credit suspension directive must be given to the secured lender contemporaneously with a request for a payoff statement or a short-pay statement in anticipation of and in preparation for the imminent settlement of the sale or new loan transaction. Pay attention to this requirement. If the credit suspension directive is provided by the settlement agent, then it must accompany a formal request for a payoff or short-pay statement pursuant to G.S. 45-36.7. It can only be sent as a "stand alone" directive to a lender if it is sent by a borrower, the legal representative of a borrower, or the attorney for a borrower.

(4) The attorney or financial institution must give a copy of the credit suspension directive to the borrower.

(5) The attorney or financial institution must provide a statutory notice to the borrower that satisfies the requirements of G.S. 45-36.7A(c). The purpose of the notice is to ensure that the borrower is aware that his line of credit will be "frozen" in anticipation of the closing of the sale or loan transaction involving his property. The notice must also advise the borrower that the borrower may instruct the attorney or financial institution that submitted the credit suspension directive to withdraw the directive at any time. However, if the borrower directs the withdrawal of the credit suspension directive, the settlement of the sale or new loan transaction may be jeopardized because the payoff or release information provided by the lender may become inaccurate.

Practice Pointer: Unless the attorney represents the borrower whose equity line of credit is to be "frozen" with a credit suspension directive, an attorney licensed to practice law in North Carolina should not issue a credit suspension directive to a lender unless and until the attorney ensures that all five of the requirements described above have been fully and carefully satisfied.

c. The duties imposed on the lender following the lender's receipt of a credit suspension directive are as follows:

(1) Subject to the exceptions noted below, the lender must suspend the borrower's right and ability to obtain credit advances which, if made, would be secured by the deed of trust. The period of suspension continues through the payoff date stated in the credit suspension directive. There are several exceptions to this rule. Notwithstanding a lender's receipt of a credit suspension directive, the lender may advance sums and incur expenses (i) for insurance, taxes, and assessments; (ii) to protect the lender's interest under the deed of trust; (iii) to preserve and protect the value and condition of the real property encumbered by the deed of trust; or (iv) to complete the construction of improvements on the real property encumbered by the deed of trust. In addition, the secured creditor may permit the borrower to obtain a credit advance, but only if the credit advance was initiated or approved before the lender received the credit suspension directive (for example, if a borrower writes a check on a home equity line of credit days before the lender receives a credit suspension directive, the lender may honor the check even if the check is presented for payment days after the lender receives the credit suspension directive).

(2) Regardless of whether the amount paid is sufficient to pay the secured obligation and other sums secured by the deed of trust in full, the lender must apply to the secured obligation all sums it subsequently receives during the period of suspension from the settlement agent or from or on behalf of the borrower. If the amount paid is sufficient to pay the loan in full, then the lender is required pursuant to G.S. 45-36.9(a) to cancel the deed of trust within 30 days. Sums paid to the lender in excess of the amount required to pay the secured obligation and other sums secured by the security instrument in full must be refunded by the lender to (or at the direction of) the person who actually paid the excess amount. This is important, because the person who actually paid the money will often be the closing attorney or settlement agent, not the borrower. Thus, if a sum greater than the loan payoff amount is wired to the bank by the set-

tlement agent and no instructions are received from the settlement agent as to the disposition of any excess sum paid, the lender must refund the excess to the settlement agent, not the borrower.

d. As a general rule, the federal truth-in-lending regulations prohibit a lender from unilaterally suspending a borrower's ability to obtain credit advances on his home equity line of credit. However, a lender may make any change to the terms of a home equity line of credit (including, presumably, suspending the borrower's ability to obtain credit advances) if "the consumer specifically agrees to it in writing at that time." To work around the constraints imposed on a lender by the federal truth-in-lending regulations, new G.S. 45-36.7A provides that if the person giving a credit suspension directive is not the borrower, then the person giving the directive is conclusively deemed to be the borrower's agent with full authority from the borrower to issue the credit suspension directive on the borrower's behalf. This provision should minimize conflict with the federal truth-in--lending regulations.

e. A credit suspension directive may be withdrawn at any time by the person who gave the directive. If the directive was given by the settlement agent (i.e., an attorney (other than the borrower's attorney) or the financial institution who will handle the consummation of the anticipated sale or loan transaction), the settlement agent must promptly notify the lender that the credit suspension notice is withdrawn if (i) requested to do so by the borrower, or (ii) the anticipated sale or loan transaction is cancelled. When the lender receives a notice from the person who originally gave the credit suspension notice that the directive has been withdrawn, the lender may lift the suspension and reinstate the borrower's right and ability to obtain additional credit advances.

A credit suspension directive is a useful pre-closing tool a closing attorney or financial institution can use to "freeze" a line of credit pending a sale or loan transaction that requires cancellation of an existing deed of trust or the release of property from the lien of an existing deed of trust. G.S. 45-36.7A can be used in connection with open-end and closed-end lines of credit, whether secured by a future advance deed of trust subject to Article 7 of Chapter 45 or an equity line of credit deed of trust subject to Article 9 of Chapter 45. If handled properly by a settlement agent, a credit suspension directive obviates the need for a subsequent request to terminate an equity line of credit.

Attachment 10 to this article is a generic "Credit Suspension Directive" that should satisfy the requirements of G.S. 45-36.7A.

Attachment 11 to this article is a generic "Notice to Borrower Regarding Credit Suspension Directive" that should satisfy the requirements of G.S. 45-36.7A(c).

Attachment 12 to this article is a combined "Request for Payoff," "Credit Suspension Directive," and "Notice to Borrower Regarding Credit Suspension Directive" for use by an attorney that should satisfy the requirements of G.S. 45-36.7 and G.S. 45-36.7A.

3. Request to Terminate an Equity Line of Credit – G.S. 45-82.2. One of the most frustrating and litigation-provoking provisions in Article 9 of Chapter 45 (the article governing equity lines of credit) is the sentence in G.S. 45-81(c) that reads as follows:

> At any time when the balance of all outstanding sums secured by a mortgage or deed of trust pursuant to the provisions of this Article is zero, the lender shall, upon the request of the borrower, 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.

On the authority of this provision and G.S. 45-36.9(a) as it currently exists, many lenders take the position that they are not required to cancel a deed of trust securing a home equity line of credit until the balance in the account is reduced to zero *and* the *borrower* has requested (some lenders contend in writing) that the deed of trust be cancelled. This provision has haunted title attorneys, title insurance companies, and lenders (who have been on both sides of the issue) for years. The amendment of G.S. 45-36.9(a) (discussed above) and a new section in Article 9 (G.S. 45-82.2, entitled "Request to Terminate an Equity Line of Credit") resolve this issue, at least with respect to deeds of trust that secure equity lines of credit. Although G.S. 45-82.2 clearly applies to deeds of trust that secure revolving lines of credit subject to Article 9 of Chapter 45 of the General Statutes (the statute that governs equity lines of credit), there is uncertainty as whether G.S. 45-82.2 applies with equal force to future advance deeds of trust subject to Article 7 of Chapter 45 (the old future advance statute).

Before turning to the details of G.S. 45-82.2, it is important to note that the definitions section in Article 9, G.S. 45-81, has been *completely* rewritten. As defined in revised G.S. 45-81, an "equity line of credit" is defined as follows:

> An agreement in writing between a lender and a borrower for an extension of credit pursuant to which (i) at any time within a specific period not to exceed 30 years the borrower may request and the lender is obligated to provide advances up to an agreed aggregate limit; (ii) any repayments of principal by the borrower within the specified period will reduce the amount of the advances counted against the aggregate limit; and (iii) the borrower's obligation to the lender is secured by an equity line security instrument.

The term "equity line security instrument" is defined as follows:

> An agreement, however denominated, that (i) creates or provides for an interest in real property to secure payment or performance of an equity line of credit, whether or not it also creates or provides for a lien on personal property; (ii) shows on its face the maximum principal amount which may be secured at any one time; and (iii) shows on its face

that it secures an equity line of credit governed by the provi sions of this Article [Article 9 of Chapter 45]. The term "equity line security instrument" includes a deed of trust and a mortgage.

With these definitions as background, let's consider the provisions of new G.S. 45-82.2, entitled "Request to Terminate an Equity Line of Credit." As contemplated by G.S. 45-82.2:

a. A "request to terminate an equity line of credit" is defined in G.S. 45-81 as a "written request submitted under G.S. 45-82.2 to a lender to terminate an equity line of credit." Although no particular phrasing is required for a request to terminate an equity line of credit and the request may take many forms, G.S. 45-82.2(b) provides a form which, if used, is sufficient to satisfy the requirements of the statute.

b. A request to terminate an equity line of credit may be submitted by any "authorized person." Under G.S. 45-81, each of the following is an "authorized person":

(1) Any borrower.

(2) The legal representative of any borrower.

(3) The attorney for any borrower.

(4) A title insurance company authorized to issue title insurance policies in North Carolina, but only when the company is acting in connection with the title insurance policy issued or to be issued with respect to property then encumbered by an existing equity line security instrument.

(5) An attorney licensed to practice law in North Carolina or a bank, savings and loan association, savings bank, or credit union, but only when the attorney or financial institution is or was responsible for the disbursement of funds in connection with the sale of, or a new loan secured by, property then encumbered by an existing equity line security instrument, and a requirement of the sale or new loan transaction is or was that the property be conveyed or encumbered free and clear of the lien of the existing equity line security instrument.

Practice Pointer: Unless the attorney represents the borrower whose equity line of credit is to be terminated, an attorney licensed to practice law in North Carolina should not issue a request to terminate an equity line of credit to a lender unless the attorney satisfies all of the requirements described above *and* gives the borrower a copy of the request sent to the lender and a copy of the statutory "Notice to Borrower" (discussed below).

c. Upon receipt from an authorized person of a request to terminate an equity line of credit, the lender is required to do all of the following:

(1) Terminate the borrower's right to obtain advances under the borrower's equity line of credit.

(2) Apply all sums subsequently paid by or on behalf of the borrower in connection with the equity line of credit to the satisfaction of the equity line of credit and other sums secured by the related equity line security instrument.

(3) When the balance of all outstanding sums secured by the related equity line security instrument becomes zero, cancel the related equity line security instrument as a matter of public record pursuant to G.S. 45-37.

d. As a general rule, the federal truth-in-lending regulations prohibit a lender from terminating a borrower's home equity line of credit unless certain conditions exist (such as the borrower's default). However, a lender may make any change to the terms of a home equity line of credit (including, presumably, terminating the home equity line of credit) if "the consumer specifically agrees to it in writing at that time." To work around the constraints imposed on a lender by the federal truth-in-lending regulations, new G.S. 45-82.2 provides that a request to terminate an equity line of credit is conclusively deemed to have been submitted by or on behalf of a borrower if it is submitted by an authorized person. This provision should minimize conflict with the federal truth-in-lending regulations.

e. As was the case with a credit suspension directive (described above), G.S. 45-82.2 requires certain classes of authorized persons to give a copy of the request and a statutory notice to the borrower if they submit a request to terminate an equity line of credit to the borrower's lender. If the request to terminate an equity line of credit is a title insurance company, the notice to the borrower must satisfy the requirements of G.S. 45-82.2(c). If the authorized person who gives the borrower's lender a request to terminate an equity line of credit is the settlement agent responsible for the disbursement of funds (i.e., an attorney (other than an attorney who actually represents the borrower) or a financial institution), the form of the notice to the borrower must satisfy the requirements of G.S. 45-82.2(d). In each case, the notice to the borrower must be accompanied by a copy of the request to terminate the equity line of credit submitted to the borrower's lender by the authorized person. The notice to the borrower explains the effect of a request to terminate an equity line of credit and the actions the borrower's lender is required to take upon receipt of the request.

The provisions of G.S. 45-82.2 provide an easy mechanism at closing to ensure the cancellation of an equity line security instrument once the balance in the account is reduced to zero. When the request is signed and submitted to the lender by an authorized person, the lender is required to terminate the borrower's right to obtain additional credit advances, apply all sums subsequently received by the lender to the satisfaction of the equity line of credit, and cancel the deed of trust securing the equity line of credit once the balance becomes zero. If the request is signed and submitted by a title insurance company or a settlement agent, the requesting party must ensure that

a copy of the request and a special notice to the borrower are delivered to the borrower.

Attachment 13 to this article is a generic "Request to Terminate an Equity Line of Credit" that should satisfy the requirements of G.S. 45-82.2.

Attachment 14 to this article is a generic "Notice to Borrower Regarding Request to Terminate an Equity Line of Credit" that should satisfy the requirements of G.S. 45-82.2(d).

Attachment 15 to this article is a combined "Request to Terminate an Equity Line of Credit and Notice to Borrower" for use by an attorney that should satisfy the requirements of G.S. 45-82.2.

4. Notice Regarding Future Advances – G.S. 45-82.3. G.S. 45-82.3 is a new statute designed to remedy a very specific problem that occasionally arises under current law. Although G.S. 45-82.3 clearly applies to deeds of trust that secure revolving lines of credit subject to Article 9 of Chapter 45 of the General Statutes (the statute that governs equity lines of credit), there is uncertainty as whether G.S. 45-82.3 applies to future advance deeds of trust subject to Article 7 of Chapter 45 (the old future advance statute).

Occasionally, the outstanding balance of an equity line of credit will be properly reduced to zero in connection with a sale or new loan transaction, but the deed of trust that secures its repayment doesn't get cancelled (as it was supposed to be). Subsequently (sometimes innocently and sometimes not), the borrower realizes the equity line of credit is still "live," and the borrower obtains additional credit advances secured by the deed of trust, thereby impairing the rights of the purchaser or new lender who expected the equity line of credit to be terminated and the deed of trust securing its repayment cancelled. Under current law, there is no ready mechanism for the innocent purchaser or lender (or the title insurance company that issued title insurance in connection with the sale or loan transaction) to determine the amount currently owing, stop the original borrower from obtaining additional credit advances, and get the property released from the deed of trust that secures the equity line of credit. G.S. 45-82.3 is a post-closing remedy for this situation.

As contemplated by G.S. 45-82.3:

a. A "notice regarding future advances" is defined in G.S. 45-81 as a "written notice submitted under G.S. 45-82.3 to a lender that prevents certain advances made pursuant to an equity line of credit from being secured by the related equity line security instrument." Although no particular phrasing is required for a notice regarding future advances, G.S. 45-82.3(e) provides a form which, if used, is sufficient to satisfy the requirements of the statute.

b. A notice regarding future advances may be submitted to a lender by any of the following:

(1) Any borrower.

(2) The legal representative of any borrower.

(3) The attorney for any borrower.

(4) A title insurance company authorized to issue title insurance policies in North Carolina, but only when the company is acting in connection with the title insurance policy issued or to be issued with respect to property then encumbered by an existing equity line security instrument.

(5) An attorney licensed to practice law in North Carolina or a bank, savings and loan association, savings bank, or credit union, but only when the attorney or financial institution is or was responsible for the disbursement of funds in connection with the sale of, or a new loan secured by, property then encumbered by an existing equity line security instrument, and a requirement of the sale or new loan transaction is or was that the property be conveyed or encumbered free and clear of the lien of the existing equity line security instrument.

Practice Pointer: Unless the attorney represents the borrower whose equity line of credit is involved, an attorney licensed to practice law in North Carolina should not issue a notice regarding future advances to a lender unless the attorney satisfies all of the requirements described above and gives the borrower a copy of the notice sent to the lender and a copy of the statutory "Notice to Borrower" (discussed below).

(6) An "owner of the property" – that is, any person owning a present or future interest in the real property encumbered by the equity line security instrument. This would include, for example, a person who purchased the property from the borrower and is surprised to learn that his property remains subject to his seller's equity line security instrument. However, the trustee in a deed of trust and the owner or holder of a mortgage, deed of trust, mechanic's or materialman's lien, judgment lien, or any other lien on, or security interest in, the real property is not considered an "owner of the property" for these purposes.

(7) A "qualified lienholder" – that is, a person who has a mortgage or deed of trust on property that is already encumbered by an existing equity line security instrument, where (i) that person's mortgage or deed of trust was recorded after the existing equity line security instrument, and (ii) it appears from warranties or otherwise that the person's mortgage or deed of trust was not intended to be subordinate to the existing equity line security instrument. As a practical matter, this means a lender who made a new loan secured by the property under circumstances in which the existing home equity line of credit was supposed to be paid in full and the deed of trust that secured its repayment cancelled.

c. Subject to certain exceptions contained in G.S. 45-82.3(c), an advance made by a lender to a borrower pursuant to an

equity line of credit will not be secured by the related equity line security instrument if the advance occurs after the lender receives a notice regarding future advances and has had not less than one complete business day to act on it. This provision "stops the bleeding" by preventing the outstanding balance of the equity line of credit from increasing further to the detriment of innocent parties. Upon receipt of a notice regarding future advances, the lender is authorized to (but is not necessarily required to) terminate the borrower's right and ability to obtain additional advances under the equity line of credit. Because the equity line of credit may be secured by other collateral or the lender may be willing to permit the borrower to obtain unsecured credit advances, the lender may elect to permit the borrower to continue obtaining credit advances – but the new advances will not be secured by the real property at issue.

d. If the person who gives the lender a notice regarding future advances is (i) a title insurance company, (ii) an attorney (other than an attorney who represents the borrower), (iii) a financial institution, (iv) an owner of the property (other than an owner who is also a borrower), or (v) a qualified lienholder, the borrower must be given a copy of the notice regarding future advances and a statutory notice. The form for the statutory notice appears in G.S. 45-82.3(f). It instructs the borrower to contact its lender to determine whether the borrower is entitled to obtain additional credit advances.

Taken together with the expansion of the list of parties entitled to obtain payoff statements, G.S. 45-82.2 and 45-82.3 will be particularly useful to title insurance companies that have issued policies to purchasers or lenders insuring that the property is no longer encumbered by a deed of trust securing a home equity line of credit. The title insurance company will be able to ascertain the amount owed, "freeze" that sum, cut off further exposure and liability, obtain a payoff statement from the lender, pay the amount owing on the equity line of credit, and compel the cancellation of the offending equity line security instrument.

Attachment 16 to this article is a generic "Notice Regarding Future Advances" that should satisfy the requirements of G.S. 45-82.3.

Attachment 17 to this artice is a generic "Notice to Borrower Regarding Future Advances" that should satisfy G.S. 45-82.3.

Attachment 18 to this article is a combined "Notice Regarding Future Advances and Notice to Borrower" for use by an attorney that should satisfy the requirements of G.S. 45-82.3. •

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"One's mind, once stretched by a new idea, never regains its original dimensions."

Oliver Wendell Holmes

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