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The NC Connection

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Exclusions Explained

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Sometimes, it's not what you have, but what you don't have, that counts. Much has been written and explained as to the importance of obtaining title insurance coverage for real estate transactions; Investors Title even has a brochure entitled "Why You Need Title Insurance" that lists the numerous matters that a title insurance policy covers for an insured lender and owner. It is also important, however, to realize that a title insurance policy contains exclusions from coverage; if an insured party submits a claim for an expressly excluded matter, then the title insurance company is not liable and will not pay attorneys' fees or other costs arising from the excluded matter. Understanding what the title insurance policy does not cover can be crucial when preparing an opinion on title as well as instructing clients as to potential areas of exposure and liability.

Exclusion #1 (2006 ALTA Loan and Owner's Title Insurance Policies)

The first exclusion in the title

insurance policy deals with matters arising from governmental regulation and laws, including zoning issues. The title insurance policy will not cover governmental laws or regulations that restrict, regulate or relate to the following:

"Understanding what the title insurance policy does not cover can be crucial..."

- a. occupancy, use or enjoyment of the Land
- b. character, dimensions or location of improvements built on the Land
- c. the subdivision of the Land

d. environmental protection issues

In addition, the title insurance policy does not cover the effect of any violations of said governmental laws or regulations. However, this exclusion shall not apply if a notice affecting the Land is recorded in the Public Records for a violation or intention to enforce the governmental law or regulation;

this exception is found in Covered Risk #5 in the title insurance policy jacket.

Please note that obtaining a zoning endorsement such as the ALTA 3-06 or 3.1-06 Endorsement does not fully supersede this exclusion. The ALTA zoning endorsements only give affirmative coverage to an Insured as to the zoning classification of the Land and the subsequent uses allowed by the zoning ordinance for the Land as of the Date of Policy.

Continued on page 2.

Commercial Services Division



Inside this issue:

Exclusions Explained	1-3
NC Fun Facts	2
RESPA Rule FAQs	4
Payments Made Under a Power of Attorney	4
Claims Corner	6
ALTA 6.2-06	6

Exclusions Explained (cont. from page 1):

Another part of the governmental exclusion deals with governmental police power. Typically, matters associated with the governmental police power are excluded from policy coverage; however, this exclusion shall not apply if a notice affecting the Land is recorded in the Public Records for exercise of a governmental police power; this exception is found in Covered Risk #6 in the title insurance policy jacket.

Exclusion #2 (2006 ALTA Loan and Owner's Title Insurance Policies)

The second exclusion from coverage is for rights of eminent domain or condemnation; however, as in the first exclusion, if a notice of eminent domain is recorded in the Public Records, then this exclusion shall not apply as stated in Covered Risk #7. Furthermore, the second exclusion is also subject to the provision in Covered Risk #8: "Any taking by a governmental body that has occurred and is binding on the rights of a purchaser for value without Knowledge."

“Real estate attorneys should pay particular attention to exclusion #3...”

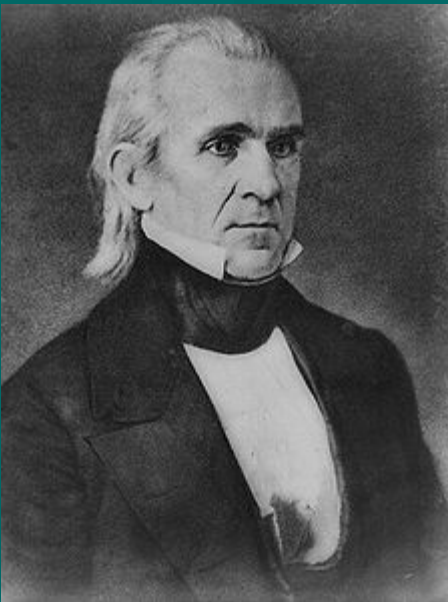
Exclusion #3 (2006 ALTA Loan and Owner's Title Insurance Policies)

The third exclusion is crucial for real estate attorneys to understand the various implications of coverage – especially when preparing opinions on title for title insurance companies. In a nutshell, the title insurance policy does not provide coverage for defects, liens or encumbrances that fit the following criteria:

- a. matters created or assumed by the Insured Claimant
- b. unrecorded matters that are not disclosed to the Company at the Date of Policy, but are known by the Insured Claimant and not disclosed in writing to the Company before the title insurance policy is issued
- c. matters that create no loss or damage for the Insured Claimant
- d. matters occurring after the Date of Policy
- e. matters that result in loss or damage because the Insured Claimant did not either pay value for the (1) Insured Mortgage (loan policy) or the (2) Title (owner's policy)

Real estate attorneys should pay particular attention to Exclusion #3(b) and the importance of disclosure of all known items affecting the Land (whether of record or not) to the title insurance company.

There is a caveat as to Exclusion #3(d) in both the Loan and the Owner's jackets. In the Loan Jacket, Covered Risks #11, #13, and #14 are not affected by Exclusion #3(d).



NC Fun Facts

James K. Polk, born in what is now known as Pineville in Mecklenburg County, North Carolina, was the eleventh President of the United States. Polk was the last strong pre-Civil War president. Polk is noted for his foreign policy successes. He threatened war with Britain then backed away and split the ownership of the Oregon region (the Pacific Northwest) with Britain. When Mexico rejected

American annexation of Texas, Polk led the nation to a sweeping victory in the Mexican–American War, followed by purchase of California, Arizona, and New Mexico. He secured passage of the Walker tariff of 1846, which had low rates that pleased his native South. He established a treasury system that lasted until 1913. Scholars have ranked him favorably on the list of greatest presidents for his ability to set an agenda and achieve all of it. Polk has been called the "least known consequential president" of the United States.

Continued on page 3.

Exclusions Explained (cont. from page 2):

Covered Risk #11 basically covers construction loan advances whereas Covered Risk #13 addresses creditors' rights issues. Covered Risk #14 addresses gap coverage for matters occurring after the Date of Policy but before the insured Mortgage is recorded. In the Owner's Jacket, Covered Risks #9 and #10 are not affected by Exclusion #3(d). Covered Risk #9 concerns creditors' rights issues, and Covered Risk #10 is gap coverage for matters that occur post-policy but before the recording of the deed or conveyance instrument.

Exclusion #4 (2006 ALTA Owner's Title Insurance Policy)

The fourth exclusion in the owner's policy addresses coverage for creditors' rights issues for the current insured transaction. The title insurance policy expressly excludes any claims arising from bankruptcy actions that characterize the current insured transaction as a fraudulent or preferential transfer. Exclusion #4 does not negate the coverage provided in Covered Risk #9 for any creditors' rights matters that occurred prior to the current insured transaction.

“Through a better understanding of the matters excluded...a real estate attorney can better advise the client...”

Exclusion #5 (2006 ALTA Loan Title Insurance Policy)

The fifth exclusion of the loan policy deals with the unenforceability of the Insured Mortgage because of a failure to abide by usury or truth in lending laws. In order to obtain affirmative coverage for Exclusion #5 in the loan policy, an ALTA 27-06 Endorsement (Usury) may be obtained by the Insured Lender.

Exclusion #5 (2006 ALTA Owner's Title Insurance Policy)

The fifth and final exclusion in the owner's policy concerns real estate tax or assessment liens that attach between the gap period of the Date of Policy and the date of recording the deed or conveyance instrument in the public records.

Exclusion #6 (2006 ALTA Loan Title Insurance Policy)

The sixth exclusion from coverage in the loan policy mirrors Exclusion #4 from the owner's policy and expressly excludes creditors' rights issues arising from the current insured transaction such as a preferential or fraudulent transfer designation in a bankruptcy action. Exclusion #6 does not negate the coverage provided in Covered Risk #13 for any creditors' rights matters that occurred prior to the current insured transaction.


Exclusion #7 (2006 ALTA Loan Title Insurance Policy)

The seventh and final exclusion in the loan policy concerns real estate tax or assessment liens that attach between the gap period of the Date of Policy and the date of recording the Insured Mortgage in the public records. However, Exclusion #7 does not affect the coverage provided under Covered Risk #11(b) which states that the title policy shall give coverage for the lack of priority of an Insured Mortgage over street improvement assessment liens for ongoing or completed construction at Date of Policy.

Through a better understanding of the matters excluded from coverage in a title insurance policy, a real estate attorney can better advise the client as to the importance of full disclosure to the title insurance company, suggest endorsements for affirmative coverage for certain exclusions in the title insurance policy, and give reasonable expectations to the client in case of a claim.

RESPA Rule FAQs

The Department of Housing and Urban Development offers a “frequently asked questions” resource regarding the RESPA Rule and the new GFE/HUD documents. The resource may be accessed by clicking this graphic or by visiting www.hud.gov/respa. Be sure to revisit the link often as new Q&As are added frequently.

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Payments Made Under a Power of Attorney

The North Carolina Court of Appeals has ruled that an agent may keep the payments she made to herself using a Power of Attorney (POA)—without authorization—because the payments had been approved as reasonable in a legal proceeding before the principal died. The case began after the death of Anges Edwards in April 2006. Prior to her death, Edwards gave her granddaughter, Jennifer Tippet, a durable POA, which was recorded in the Register of Deeds office in July 2001. Edwards suffered from Alzheimer's, and by October 2001, she was incompetent. Not until September 2004, did the Cumberland County Clerk of the Superior Court conduct an audit. In October 2004, Tippet filed her first accounting (although this one covered almost three years) showing total distributions to Tippet of \$32,800. In August 2005, the clerk entered an order finding that Tippet was entitled to payment for her services and that she had violated her fiduciary duties by not obtaining the clerk's approval for the payments. Nevertheless,

the clerk found that the payments were reasonable. After Edwards died intestate in April 2006, the Administrator of her estate filed a Motion for Relief, specifically seeking to set aside the Clerk's order. That Motion was denied by the assistant clerk of the superior court in October 2007, and the Superior Court of Cumberland County entered an order upholding the denial. The Administrator appealed, but the appellate court affirmed. In reaching that outcome, the Court concluded, “If the clerk of superior court can grant approval prospectively, then the clerk of superior court can grant approval retroactively.” Since, the Court concluded, the clerk of superior court is charged with that duty under N.C. Gen. Stat. Sec. 7A-103(15), then “[i]nherent in this authority is the power to approve or disapprove financial arrangements between the principal and attorney-in-fact.” --*In re Edwards*, No. COA09-329, N.C. Ct. App. 3/2/10

The information contained in this article is not to be construed as legal advice.

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- 4 (1 hour) Courses 1:00 – 5:30 pm
- Cocktail Reception 5:30 – 8:30 pm

Saturday:

- Registration and Breakfast 7:30 – 7:45 am
 - 2 (1 hour) Courses 7:45 – 10:00 am
 - Pre-Game Tailgate Party at the Investors Title Corporate Office (time TBD)
 - UNC vs. Clemson Football Game (time TBD)
- Ticket availability is limited to 2 per seminar attendee. Reserve tickets early.**

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Small Details Lead to Big Problems in Bankruptcy Court

Part 1

By Robert Crabill, Title Attorney
& Risk Control Manager

When To File
a Claim

Contacting the
Claims
Department

Frequently
Asked
Questions

File a Claim

Lenders often deliver closing documents at the last minute. The note and deed of trust may have blanks to be completed prior to closing. The dates or loan information may be pre-printed on the documents. Under rushed

conditions, the documents may not always be carefully reviewed. Years later the borrower may default and seek protection in bankruptcy court. When the lender seeks to enforce its lien, the bankruptcy trustee will review the documents to see if the lender is properly secured. When this happens, seemingly small details can become major problems for lenders seeking to enforce a lien.

One case that increased concern for lenders is Beaman v. Head, 353 B.R. 122 (Bankr. E.D.N.C. 2006). In this case, the debtor executed a note for \$180,515.75 on July 29, 1998. The deed of trust securing this debt referred to a “promissory note of even date herewith.” The deed of trust, however, was dated July 28, 1998. Based on the one day discrepancy between the documents, the court ruled that the deed of trust could be invalidated when it referred to an incorrect date for the promissory note.

These dates may have been pre-printed and not reviewed prior to closing. Eight years later, the one day difference resulted in a lender not having a valid security interest. This ruling also set the stage for a climate where deeds of trust will be scrutinized down to the smallest details. This series will illustrate three specific instances where security instruments have been challenged in bankruptcy court and have led to lender claims for Investors Title.

In the first example, two borrowers executed a promissory note in the amount of \$225,000 on October 25, 2007. The note was secured by a deed of trust executed by the borrowers and dated October 29, 2007. This deed of trust referred to a promissory note dated October 29, 2007 in the amount of \$230,000. Investors Title provided a lender’s policy in the amount of \$230,000.

Approximately two years later, the note was in default and one of the borrowers filed a bankruptcy petition. The lender asked the bankruptcy court for permission to proceed with foreclosure, and the bankruptcy trustee objected. The basis for the bankruptcy trustee’s objection was that the inconsistent dates and loan amounts invalidated the lien. The lender filed a title claim. Investors Title was forced to pay tens of thousands of dollars to settle with the bankruptcy trustee and protect the lender’s security interest.

ALTA 6.2-06 ENDORSEMENT

This endorsement includes features commonly related to negative amortization and is designed for use when the insured variable (adjustable) rate mortgage includes provisions for changing the rate of interest; charging interest on interest; or increasing the unpaid principal balance of the loan by the addition of unpaid interest.

The typical requirement that must be satisfied prior to issuance of the 6.2-06 endorsement reads as follows:

Upon receipt of confirmation that the insured mortgage will be securing a loan with negative amortization, an ALTA 6.2 – Variable Rate Mortgage – Negative Amortization Endorsement in the form attached hereto, but completed as appropriate, will be attached to the final loan policy.