

**DEBT DESCRIPTION IN DEED OF TRUST – WHAT DEBT AND WHOSE DEBT;
CERTAIN LAND DESCRIPTION PROBLEMS**

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Adequate description of the indebtedness and the real property is important. That includes *what* indebtedness and whose. Where a deed of trust dated July 28, 1998 stated that it was given as security for a “Promissory Note of even date herewith” and the actual note dated July 29, 1998 referred to the grantor of the deed of trust and the beneficiary and to the amount referenced in the deed of trust as the amount secured, the bankruptcy court held that the deed of trust’s reference to the “Promissory Note of even date herewith” did not properly identify the secured indebtedness and the deed of trust was not enforceable against the bankruptcy trustee’s strong arm powers as a hypothetical lien creditor under 11 U.S.C.A § 544. *In re Head Grading Co., Inc.*, 353 B.R. 122 (Bankr.Ct. E.D.N.C. 2006), citing *In re Foreclosure of Deed of Trust of Enderle*, 110 N.C. App. 773, 431 S.E. 2d 549 (1993) (deed of trust referenced the securing of a debt owed by the deed of trust’s grantor but the debt was owed by a party other than the grantor and, therefore, the deed to trust was invalid); *Seventeen South Garment Co., Inc. v. Centura Bank*, 145 B.R. 511 (E.D. N.C. 1992) (use of a trade name as opposed to a corporate name in financing statement was insufficient in an 11 U.S.C.A. § 544 case); and *Putnam v. Ferguson*, 130 N.C. App. 95, 502 S.E. 2d 386 (1998) (deed of trust given by grantor that did not specifically reference the obligor of the secured indebtedness was invalid where the obligor and the grantor were different parties). See *Restatement (Third) of Property (Mortgages)* §1.3 discussing mortgages securing obligations of “non-mortgagors.” Also, see *Washington Mutual Bank, FA v. Hargrove*, _____ N.C. App. _____, 609 S.E. 2d 454 (2007), where the deed to the defendant erroneously described Lot 17 and was recorded; then the deed of trust correctly describing Lot 13 was recorded and then a correction deed correctly describing Lot 13 was recorded. The deed of trust was not rerecorded. It was held that the deed of trust was a valid lien against Lot 13. However, it is important to note that priorities were not involved. See *Restatement of the Law (Third) of Property (Mortgages)* § 1.5 entitled, “Description of the Mortgagee and the Mortgage Obligation.” See J.C. Murray, *Defective Real Estate Documents: What Are The Consequences?*, 42 Real Prop. Probate & Trust J. 367 (Summer 2007).

Where the borrower is the same as the property owner (for example, where the property owner is submitting the described land as security for debt of the property owner signing only the hypothecated security addendum), problems can arise. Even aside from the legal issues (whether the note is properly identified under the *Enderle* case cited above or the addendum contains sufficient granting language, is adequately referenced in the deed of trust itself, etc.) *the Registers of Deeds and the School of Government have taken the position that they do not index addenda and, therefore, even on request, most will not index the document in the name of the property owner signing the addendum.* So the attorney must be careful that the *property owner is shown as a grantor of the deed of trust itself and actually signs and has the property owner’s signature notarized on the deed of trust, not just the addendum.* Otherwise, the deed of trust will be treated as if unrecorded within the chain of title of the property owner and its lien priority and notice are not protected under G.S. 47-20.

In *Hudson v. Hudson*, ____ N.C. App. _____, 642 S.E. 2d 485 (2007), deficiencies in the legal description were shown to be problematic. There, a deed of trust which contained no description of the real property at the time of conveyance violated the Statute of Frauds in G.S. 22-2 and was void.

The court in *In re Law Developers, LLC*, 2008 WL 2570863 (Bankr. E.D.N.C. 2008), dealt with the following facts: On January 12, 2006, the debtor, Law Developers, executed to the bank a note and deed of trust for \$194,500 which was recorded in Brunswick County. The deed of trust’s legal description incorrectly identified the lot as Lot 43 of Cedarwood Village, whereas the intended description, as shown on page one of the deed of trust, was Lot 17 of Cedarwood. All parties agreed that Lot 17 was correct, since the debtor had sold Lot 43. The debtor filed a Chapter 11 petition in bankruptcy on February 14, 2008 and contended that the bank’s claim should be unsecured and not secured. The bank wanted to reform the deed of trust; the debtor sought to invalidate the deed of trust due to a faulty legal description. Under North Carolina law, a deed purporting to convey an interest in land is void unless it

contains a description of the land sufficient to identify it or refers to something extrinsic by which the land may be identified with certainty. *Overton v. Boyce*, 289 N.C. 291 (1976). The description in the deed of trust must be either certain itself or capable of being reduced to a certainty by a recurrence to something extrinsic to which the deed refers. *Duckett v. Lyda*, 223 N.C. 356 (1943). In *In re Law Developers*, the deed of trust referred to both Lots 17 and 43 of Cedarwood Village. It was not clear from the face of the document which lot was intended to be encumbered by the deed of trust. In addition, the deed of trust did not refer to anything extrinsic that would explain the ambiguity, for example, a prior deed. Therefore, the court held that the deed of trust, as written, was void under North Carolina law as the document failed to provide an adequate description of the encumbered lot.

Given invalidity of the deed of trust due to the legal description, the bank sought to reform the deed of trust under North Carolina law. However, North Carolina law provides the general rule that reformation will not be granted if the rights of an innocent bona fide purchaser, or someone occupying a similar status, would be prejudiced. *Hice v. Hi-Mil, Inc.*, 301 N.C. 647, 653 (1981). Therefore, a reformation is inappropriate if the debtor qualifies as a bona fide purchaser for value, or someone occupying a similar status, whose rights would be prejudiced by reforming the deed of trust to encumber Lot 17. 11 U.S.C.A §544(a)(3) provides that “[t]he trustee shall have, as of the commencement of the case, ... the rights and powers of ... a bona fide purchaser of real property.” Therefore, in Chapter 11, a debtor-in-possession has the power to avoid a claim that could be voidable by a bona fide purchaser for value at the time of the filing of the bankruptcy petition. *In re Hartman Paving Inc.*, 745 F.2d 307, 309 (4th Cir. 1984). However, the Fourth Circuit, in a heavily criticized opinion, had held that a debtor-in-possession, acting as a bona fide purchaser pursuant to 11 U.S.C.A. §544(a)(3), cannot invalidate a deed of trust where the debtor is an original party to the deed to trust and has actual notice of its existence. Thus, a Chapter 11 debtor’s actual notice of a mistake in a deed of trust is imputed to the debtor-in-possession acting as a bona fide purchaser for value. A debtor-in-possession with notice of the deed of trust is not “innocent” and therefore cannot prevent reformation of the deed of trust under North Carolina law, so the *In re Law Developers, LLC* court was obligated to follow the Fourth Circuit’s opinion in *In re Hartman Paving, Inc.*

However, the *In re Law Developers, LLC* court cited 11 U.S.C.A. §544(a)(1), another prong of the trustee’s strong arm powers which the debtor in possession can also avail itself of pursuant to 11 U.S.C.A. §1107. It is noted that while 11 U.S.C.A. §544(a)(3), discussed above, referring to a trustee’s, and therefore also a debtor-in possession’s, status as a “bona fide purchaser of real property,” and that status requires no knowledge on the part of the debtor-in-possession as discussed above, 11 U.S.C.A §544(a)(1) contains no “bona fide” status requirement. 11 U.S.C.A §544(a)(1) gives the trustee, and therefore a debtor-in-possession due to 11 U.S.C.A §1107, the status of the judicial lien creditor. Therefore, the *In re Law Developers, LLC* court found *In re Hartman Paving, Inc.* inapplicable, and instead followed *In re Millerburg*, 61 B.R. 125 (Bankr. E.D.N.C. 1986), and held that the bank’s deed of trust could not be reformed against the debtor-in-possession because of his status under 11 U.S.C.A §544(a)(1) as a protected hypothetical “judicial lien creditor,” regardless of the fact that the debtor was a party to the deed of trust and knew of the mistake. Therefore, the bank’s deed of trust was voided under 11 U.S.C.A. §544(a)(1).

Where a mistake in the acreage was discoverable in the chain of title, the bank holding a deed of trust on too many acres foreclosing and selling the property to Gray was allowed to reform the instruments to reflect that Gray should own 2.6 acres and Garrens should own 1 acre. *Citifinancial Mortgage Co. v. Gray*, ___ N.C. App. ___, 652 S.E. 2d 321 (2007).

See E. Urban, [Deeds of Trust-Failure To Name Trustee](#). The article discusses in detail the “scrivener’s error statute” in G.S. 47-36.1 prior to its 2008 amendment and the need for statutory clarification of that statute and the entire area of omitting the name of the trustee. See on that same website, E. Urban, *Recording Act Changes – New Statutes*, discussing revised G.S 47-36.1. Now, as in the past, G.S. 47-36.1 cannot be used to cure instruments that are, in some way, invalid.