INTEROFFICE MEMORANDUM

TO: Professor Forquer

FROM: Matt Stiles

DATE: November 2, 2016

RE: Precedent on foreclosure deficiency when Deed of Trust not signed under seal

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The statutes governing foreclosures can be found in §§ 45-21.1 to 45-21.38 of the North Carolina General Statues. The following discussion analyzes the precedent set through the application of these statutes.

FACTUAL BACKGROUND

The following factual background defines some relevant terms.

- *Deed of Trust*

North Carolina is a title theory jurisdiction, by which a deed of trust passes title to a trustee for the benefit of the lender. A deed of trust is a type of secured real-estate transaction. A deed of trust involves three parties: a lender, a borrower, and a trustee. The lender gives the borrower money. In exchange, the borrower gives the lender a promissory note. As security for the promissory note, the borrower transfers a real property interest to a third-party trustee. Should the borrower default on the terms of his loan, the trustee may take full control of the property to correct the borrower's default.[1] While North Carolina recognizes mortgages, the prevailing practice is to use a deed of trust to encumber real property. Although North Carolina is a title theory jurisdiction, the grantor retains the right to possession at least until default.[2]

- *Anti-deficiency laws*

When the total mortgage debt exceeds the foreclosure sale price, the difference is called a "deficiency." In North Carolina, the foreclosing party can get a deficiency judgment after a non-judicial foreclosure, except in certain instances. For example, the lender cannot seek a deficiency judgment after a non-judicial foreclosure of a purchase money (seller financed) deed of trust. N.C. Gen. Stat § 45-21.38. The foreclosing party may also be barred from seeking a deficiency

[1] https://www.law.cornell.edu/wex/deed_of_trust

[2] http://crlaw.com/news/wp-content/uploads/2012/01/North-Carolina-Lending-Law-A-Guide-for-Commercial-Lenders-and-Businesses.pdf

judgment in certain cases when the deed of trust is nontraditional (for example, Pick-a-Payment or Option ARM loans), and secures the borrower's principal residence. N.C. Gen. Stat. § 45-21.38A.[3]

- *Defenses to a Deficiency Suit*

North Carolina provides borrowers with a statutory defense against a deficiency lawsuit. If the lender is the purchaser of the borrower's home at the foreclosure sale, the borrower may defeat or offset any alleged deficiency by showing that the home's fair market value equaled the amount of the outstanding mortgage or that the amount bid by the lender at the sale was substantially less than the value of the home.[4]

QUESTION PRESENTED

In North Carolina case law, is there precedent establishing that a deed of trust in foreclosure deficiency, which was not signed under seal and is now released, is subject to a 3-year statute of limitations?

BRIEF ANSWER

NO. In North Carolina, statutory law establishes that if a promissory note is secured by a deed of trust, an action on the note is subject to a three-year statute of limitations.[5] However, there is no precedent that establishes a three-year statute of limitations on a deed of trust in foreclosure deficiency, which was not signed under seal and is now released.

Once a foreclosure is complete, if a balance remains on the debt the lender may seek a judgment against the borrower in the amount of the deficiency. *See Blanton v. Sisk*, 70 N.C.App. 70, 71, 318 S.E.2d 560, 562 (1984). A deficiency judgment imposes personal liability on the borrowers for the difference between the amount of the debt and the amount yielded by the foreclosure sale. *See Hyde v. Taylor*, 70 N.C.App. 523, 526, 320 S.E.2d 904, 906 (1984).

The statute of limitations does not begin to accrue on the date of default (last payment),

[3] http://www.alllaw.com/articles/nolo/foreclosure/laws-in-north-carolina.html
[4] N.C. Gen. Stat § 45-21.36.
[5] https://advance.lexis.com/document/?pdmfid=1000516&crid=92a61f61-27b3-4071-a500-821c24242c63&pddocfullpath=%2Fshared%2Fdocument%2Fanalyticalmaterials%2Furn%3AcontentItem%3A545M-WSG0-R03M-238P-00000-00&pddocid=urn%3AcontentItem%3A545M-WSG0-R03M-238P-0000000&pdcontentcomponentid=268898&pdteaserkey=sr0&ecomp=q85tk&earg=sr0&prid=6ff7515e-e277-427b-b0ed-4c8037aca563

but instead begins on the date of maturity of the loan, unless the note holder has exercised his right of acceleration. However, if payment on a promissory note is accelerated, the power of sale would begin to run on the date of acceleration.[6]

The three-year statute of limitations barring an action directly upon the note will not usually bar a foreclosure on the deed of trust securing that note. If a simple note is secured by a deed of trust, the fact that an action is barred on the note because the three-year statute of limitations has run against the note will not preclude foreclosure on the deed of trust securing the note, provided the ten-year limitations period for the foreclosure has not yet run.[7]

The party in default should know that foreclosure by action may be barred where the grantor in a deed of trust has been in actual possession of the mortgaged land for more than ten years after default, after the power of sale became absolute, or after the last payment was made on the mortgage indebtedness. The Court of Appeals has explained that two elements are required to bar a foreclosure under this limitations provision. First, ten years must have passed after the occurrence of one of the statute's triggering events—i.e., the date of forfeiture, the date the power of sale became absolute, or the date the last payment was made. Second, the mortgagor must have remained in absolute possession of the property at issue during the entire ten-year period.[8]

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[6] https://advance.lexis.com/document/documentlink/?pdmfid=1000516&crid=cb55ab93-1555-49fe-8268-27ce72225b75&pddocfullpath=%2Fshared%2Fdocument%2Fcases%2Furn%3AcontentItem%3A5FTJ-0NP1-F04HF07F0000000&pdcontentcomponentid=9108&pddoctitle=In+re+Foreclosure+of+Deed+of+Trust+Executed+by+Brown%2C+___+N.C.+App.+___%2C+771+S.E.2d+829+(2015)&ecomp=h35Lk&prid=92a61f61-27b3-4071-a500-821c24242c63

[7] https://advance.lexis.com/document/?pdmfid=1000516&crid=92a61f61-27b3-4071-a500-821c24242c63&pddocfullpath=%2Fshared%2Fdocument%2Fanalyticalmaterials%2Furn%3AcontentItem%3A545M-WSG0-R03M-238P-00000-00&pddocid=urn%3AcontentItem%3A545M-WSG0-R03M-238P-0000000&pdcontentcomponentid=268898&pdteaserkey=sr0&ecomp=q85tk&earg=sr0&prid=6ff7515e-e277-427b-b0ed-4c8037aca563

[8] https://advance.lexis.com/document/?pdmfid=1000516&crid=92a61f61-27b3-4071-a500-821c24242c63&pddocfullpath=%2Fshared%2Fdocument%2Fanalyticalmaterials%2Furn%3AcontentItem%3A545M-WSG0-R03M-238P-00000-00&pddocid=urn%3AcontentItem%3A545M-WSG0-R03M-238P-0000000&pdcontentcomponentid=268898&pdteaserkey=sr0&ecomp=q85tk&earg=sr0&prid=6ff7515e-e277-427b-b0ed-4c8037aca563

CONCLUSION

The Supreme Court of North Carolina has found that N.C.G.S. § 45-21.36 represents an exercise of equity. The statute recognizes the validity of powers of sale contained in deeds of trust, but regulates the exercise of such powers by the application of well-settled principles of equity. *See Richmond Mortg. & Loan Corp. v. Wachovia Bank & Trust Co.*, 210 N.C. 29, 34-35, 185 S.E. 482, 485 (1936). As an exercise of equity, it limits the rights of the lender so as to prevent his obtaining more than his due. *See Id.*

In 2015, the North Carolina Court of Appeals ruled consistent with the principles of equity espoused by the Supreme Court. In *United Community Bank v. Wolfe*, the court held that lenders will almost always have to go through a full jury trial in order to obtain a deficiency judgment. This holding establishes a strong deterrent against a lender pursuing an otherwise collectible foreclosure deficiency.[9]

[9] http://www.jdsupra.com/legalnews/it-just-got-harder-to-get-a-deficiency-16918/