Daily Development for Thursday, September 9, 2010
by: Patrick A. Randolph, Jr.
Elmer F. Pierson Professor of Law
UMKC School of Law
Of Counsel: Husch Blackwell Sanders
Kansas City, Missouri
dirt@umkc.edu

MORTGAGES; FORECLOSURE; FUTURE ADVANCES; PROTECTION OF SECURITY: A lender who forecloses on a deed of trust is secured not only as to the amount of debt secured by its original deed of trust, but also for amounts advanced by such lender to pay off debts secured by a prior deed of trust, notwithstanding the existence of a recording tax requirement..

Higdon v. Regions Bank, ___ S.W.3d ___ (Tenn. Ct. App. 2010). (Another aspect of this case will be the subject of tomorrow's DD)

Stinnetts financed their purchase of the Property it through a secured loan from Bank, which recorded a deed of trust against the Property. In April 1998, the Stinnetts refinanced the Property with a loan obtained from ORNL, and the Bank deed of trust was released. On September 9, 1999, Weather Tamer advanced additional money to the Stinnetts, secured by a deed of trust which was subsequently assigned to KeyBank USA, N.A. Finally, on September 20, 1999, the Stinnetts obtained another loan from ENM, Inc. Such loan was secured by a third deed of trust which was subsequently assigned to Regions Bank ("Regions").

While the Regions deed of trust was executed after the KeyBank deed of trust, Regions recorded its deed of trust prior to KeyBank, thereby making the Regions lien prior to the KeyBank lien.

In August 2001, Regions satisfied the debt secured by the ORNL deed of trust in order to stop an impending foreclosure sale. The Stinnetts filed a Chapter 13 bankruptcy petition in 2001, and the Property was subsequently sold to Jon Higdon at a foreclosure auction conducted on behalf of KeyBank on November 8, 2007. Prior to purchasing the Property, Higdon did not contact the Stinnetts or Regions Bank to ascertain the payoff amount of the Regions loan. After Higdon took title to the Property, Regions notified Higdon's attorney that Higdon's failure to resolve the deed of trust default would result in the acceleration of the mortgage debt. The default was not cured and Regions accelerated the deed of trust on April 6, 2008.

Higdon filed a complaint requesting an injunction against Regions prohibiting it from completing the foreclosure sale until the amount secured by the Regions deed of trust was judicially determined, which the court issued. In Regions' answer, it asserted a security interest in the rents generated by the Property and claimed its deed of trust secured not only its original debt (plus interest and costs), but also the amount Regions advanced for the payoff of the ORNL debt. The trial court found that the amount secured by the Regions deed of trust included the amount advanced to ORNL. Higdon appealed to Tennessee Court of Appeals.
On appeal, Higdon argued that Regions' claim was limited to the indebtedness amount on which it paid recordation tax, and that he was not liable for rent

payments made to him because of his absence of contractual privity with Regions. Therefore, the issues addressed by the court were (1) whether Regions was secured for the amount of its original debt plus the amount of indebtedness paid by Regions to release the ORNL deed of trust, and (2) whether Higdon was liable to Regions for payment of rent pursuant to the Regions deed of trust, despite the fact that Higdon was not a party to such instrument.

Regarding the amount of the debt secured by the Regions deed of trust, the court noted that Higdon's primary argument relied on precedent established prior to the Tennessee legislation's amendments of the statutes requiring the payment of mortgage registration tax. Prior to such amendments in 1987, Tennessee courts had held that "any indebtedness beyond the amount for which mortgage recording tax was paid constituted a nullity." Therefore, prior to 1987, lenders' security would be limited to the amount of principal indebtedness recorded in their deed of trust, and any protective advances made by a lender would not "relate back to the time of the original loan as to give it priority." However, subsequent to the 1987 amendments, the statutes provided in part that "[n]onpayment or underpayment of tax on an indebtedness . . . shall not affect or impair the effectiveness, validity, priority, or enforceability of the security interest or lien created or evidenced by the instrument, it b eing declared the legislative intent that the effectiveness, validity, priority, and enforceability of security interests and liens are governed solely by law applicable to security interests and liens."

The legislative amendments, coupled with the fact that the Regions deed of trust included a future advances clause providing that the deed of trust would also secure "the payment of all other sums, with interest thereon, advanced in accordance herewith to protect the security of this Deed of Trust," resulted in the court holding that Regions' payment of the ORNL deed of trust to prevent a foreclosure sale "was secured by the future advances clause in [Regions'] original Deed of Trust" and the trial court "did not err in holding that [Regions] was secured for the amount of its original debt in addition to the amount of indebtedness paid by Regions Bank to release a prior deed of trust."

Comment: Note that the Regions apparently paid off the ORNL subsequent to the creation of the lien under which Mr. Higdon purchased. Undoubtedly, by the time Regions mad such payment, it was aware of the KeyBank mortgage. Why wasn't this payoff deemed an "optional advance" and therefore in junior priority to Mr. Higdon? Tennessee apparently has abandoned the "optional/obligatory" test by statute and now permits future advance clauses to enjoy the priority of the date of their creation and recording regardless of the fact that they might constitute "optional advances." This approach, generally, is also that taken by the new Restatement of Mortgages.

Parties posting messages to DIRT are posting to a source that is readily accessible by members of the general public, and should take that fact into account in evaluating confidentiality issues.

ABOUT DIRT:

DIRT is an internet discussion group for serious real estate professionals. Message volume varies, but commonly runs 5 to 15 messages per work day.

DIRT Developments are posted periodically, as supply dictates.

To subscribe, send the message

subscribe Dirt [your name]

to

listserv@listserv.umkc.edu

To cancel your subscription, send the message signoff DIRT to the address:

listserv@listserv.umkc.edu

for information on other commands, send the message Help to the listserv address.

DIRT has an alternate, more extensive coverage that includes not only commercial and general real estate matters but also focuses specifically upon residential real estate matters. Because real estate brokers generally find this service more valuable, it is named "BrokerDIRT." But residential specialist attorneys, title insurers, lenders and others interested in the residential market will want to subscribe to this alternative list. If you subscribe to BrokerDIRT, it is not necessary also to subscribe to DIRT, as BrokerDIRT carries all DIRT traffic in addition to the residential discussions.

To subscribe to BrokerDIRT, send the message

subscribe BrokerDIRT [your name]

to

listserv@listserv.umkc.edu

To cancel your subscription to BrokerDIRT, send the message signoff BrokerDIRT to the address:

listserv@listserv.umkc.edu

professional continuing education, provided that no charge is imposed for such distribution and that appropriate credit is given to Professor Randolph, any substitute reporters, DIRT, and its sponsors.

DIRT has a WebPage at:
http://dirt.umkc.edu/