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**1. Phil owns Lot 7.**

Texas uses a race-notice theory in recording statutes. A recorded deed gives constructive notice of the deed holder's interest in the property to all subsequent transferees, that is to say, a transferee has the duty to do a record search for potential defects in the title. If a deed is not recorded, then a subsequent purchaser for value will have superior interest in the property if she gives value for the property and had no actual, constructive, or inquiry notice of another's interest in the property. Inquiry notice means that there are conditions of the property that would make a reasonable person think, "hey, maybe someone else owns the property, and I should ask about it?" One example of inquiry notice is if there has been substantial improvements on the property by a third party or another use of the property that is inconsistent with the record owner's ownership.

A purchaser at a foreclosure sale takes the property free of all encumbrances and obligations except for those encumbrances and obligations that are senior to the interest being foreclosed upon. Texas does not recognize a statutory redemption right, meaning no paying off the debt to get the property back if it has already been sold in a foreclosure sale.

Bea acquired her warranty deed on Lot 7 in 2007, but she did not record her deed until January 2010. Terry acquired her warranty deed in Lot 7 later, in 2008. But, unlike Bea, Terry did record her deed and the deed of trust immediately (the fact pattern does not say exactly when, but sounds like it was immediately recorded after the deed was conveyed, or at any rate, before Bea recorded). Neither Terry or the Lender had notice of any kind of Bea's interest in the property, as in 2008 Bea has not recorded her deed and the Developer failed to note the sale to Bea in his records. Also, Bea's only activities on Lot 7 was planting a tree and mowing the grass. The mere presence of a tree (which could be there naturally) and cut grass (the developer could be doing it), is probably not enough to constitute inquiry notice to Terry or the Lender. Now, if Bea had, say, built a huge house on Lot 7 with a sign that says "This is Bea's House," then the analysis might go differently.

As it is though, Terry's interest in Lot 7 has priority over Bea's. She gave value for Lot 7 through the mortgage secured by the deed of trust. She also purchased the property without any sort of notice that someone else owns Lot 7: There was no actual notice (Terry didn't personally know Bea owned it), no constructive notice (a search of the title records of Frio County would not have revealed Bea's deed), and

no inquiry notice (no major improvements or other obvious conditions of ownership by another on Lot 7). It can also be inferred from the facts that Terry recorded her deed prior to Bea did, since Bea did not record until January 2010. Therefore, Terry's interest is superior to Bea's.

Moving on: Terry's ownership of Lot 7 has passed to Phil, through a non-judicial foreclosure sale that was valid under Texas law. A foreclosure sale extinguishes the encumbrance for which the property is being foreclosed upon, as well as all junior liens and encumbrances. Because Bea's interest is "junior" to Terry's and the Lender's, Phil takes Lot 7 free of Bea's interest in the property when he purchased it from the foreclosure sale. In fact, he takes Lot 7 free of everyone's interests except maybe for the federal tax lien and for other undiscovered encumbrances that may be senior to the Lender's deed of trust. In any case, absent additional facts, Phil now owns Lot 7, as Bea, Terry, and the Lender's rights have been extinguished in the foreclosure sale.

## **2. Lender is not obligated to reimburse Phil for the payment of the federal tax lien.**

A purchaser at a foreclosure sale takes the property "as-is," meaning that no warranties of title is granted with the sale of property. Caveat emptor is still alive and well in a foreclosure sale.

Having purchased Lot 7 from the foreclosure sale, Phil would have taken title to Lot 7 free of all liens and encumbrances junior to the Lender's interests. However, that does not mean Phil gets a warranty deed from Lender. Indeed, the deed Phil gets at a foreclosure sale is closer to a quitclaim deed, as absolutely no warranty of title is made by anybody when property is transferred via foreclosure sale. In this situation, Lender is not responsible for any defects in Lot 7's title.

Phil should have searched the Real Property Records of Frio County BEFORE he purchased Lot 7. Had he done so, he might not have chosen to not purchase Lot 7 because of the federal tax lien. But he did purchase it, and at a foreclosure sale, he purchased Lot 7 "as-is." He might not have had to pay the federal tax lien, but we need not analyze that here because, having paid the tax lien, Phil cannot seek reimbursement from the Lender for the amount of tax lien.

**END OF EXAM**

9)

1. Phil is the true owner of Lot 7.

Under the Texas Property Code, Texas uses a notice statute, which means that a good faith purchaser who pays value and takes without notice will prevail. No recording is necessary except to put the world on notice that you are the true owner of the property.

Notice can be proved by actual notice, inquiry notice, or constructive notice. Actual notice is where the party actual knows. Inquiry notice is where the party knows of some facts that would cause a reasonable person to inquire further about the facts or situation. Constructive notice is where a deed is recorded, but the party simply fails to check the county records.

Here, starting from Terry's purchase of Lot 7 from the developer, he had no actual, constructive, or inquiry notice about Bea's ownership to the property. There was no actual notice because he did not know, and there was no constructive notice because Bea's deed had not been recorded. There was no inquiry notice because the facts state that Bea only mowed the grass and planted a tree on the property. This is insufficient to cause a reasonable person to inquire further about the activities on the property. Therefore, Terry took the property without notice and became the true owner of the property. He paid value for it in good faith and took without notice.

Once Bea recorded her warranty deed in January 2010, her deed was a wild deed and was outside the chain of title. Although she recorded prior to the judicial sale, a purchaser of property only needs to check the chain of title back from the person he/she is purchasing property from. If Phil were to check his title back from Terry, he would see that it went back to Developer, who was the original grantor. Subsequently, the lender foreclosed on the property and sold it to Phil at the sale, who also paid value in good faith and took without notice.

Therefore, Phil became the true owner after the purchase of the property from Terry.

2. Lender is not obligated to reimburse Phil because they did not warrant to defend against any subsequent claims against Lot 7. At issue is whether the lender has the obligation to reimburse Phil

because he had to pay the tax lien to avoid being foreclosed upon.

Under the Texas Property Code, a general warranty deed generally warrants (i) warranty the right of seisin/right to convey; (ii) warranty against encumbrances; (iii) warranty of quiet enjoyment; and (iv) warranty of further assurances. The warranty of the right of seisin/right to convey and the warranty against encumbrances, if breached at all, can be sued upon immediately. The warranty against encumbrances and the warranty of quiet enjoyment can only be sued upon if you are later challenged with regard to your ownership of the property. The warranty of quiet enjoyment is a warranty by the grantor that he/she will defend any subsequent claims against the property. The warranty of further assurances warrants that the seller will do anything it needs to do that it forgot to do at closing or the like.

The lender did not warrant these things, but rather Terry, through trustee, provided what equates to a warranty of quiet enjoyment. Therefore, the lender has not warranted anything and cannot be required to reimburse Phil for the tax liens that he had to pay. Phil may be able to sue Terry through the warranty and require Terry to reimburse him for the tax liens that were placed upon the property for his failure to pay taxes.

**END OF EXAM**

9)

(1) Phil owns Lot 7. Terry obviously does not own the property because he lost his equitable ownership in Lot 7 when he failed to pay on the promissory note and Trustee foreclosed on the property in a proper action. Texas has a notice recording act that protects subsequent bona fide purchasers for value and without notice against unrecorded interests in real property. This protection extends to mortgagors and lenders who lend through deeds of trust. Notice can be actual, inquiry, or record. When Terry purchased Lot 7 in 2008 and executed the deed of trust with Lender, the Bea's purchase of Lot 7 was unrecorded. Lender lacked actual notice of Bea's prior purchase. And nothing about Lot 7 would have put Lender on inquiry notice. Bea had not fenced in the property and the mowed lawn would not have been obviously indicative of ownership by Bea. An individual inspecting the property could have easily assumed that Developer mowed the lawn to keep the neighborhood looking presentable or that neighbors (including Bea) were doing so to keep the neighborhood looking respectable. Nothing in the facts suggests the tree growing on the property would have given a reasonable person reason to suspect someone already owned Lot 7 either. Lender's conveyance of the purchase price to Terry in exchange for the deed of trust qualifies as a purchase for value. The Lender thus qualifies as a bona fide purchaser for value and without notice of Lot 7.

The issue is whether Phil can claim the protections of a bona fide purchaser. He cannot do so directly because when he purchased the property in March of 2010, Bea's warranty deed on Lot 7 was properly recorded. That gave Phil record notice of Bea's ownership. But Texas recognizes the shelter rule, under which someone who acquires property from a bona fide purchaser, whether by purchase, gift, or otherwise, is sheltered by the bona fide purchaser's protections and treated like a bona fide purchaser. If it were otherwise, bona fide purchasers would not be fully protected by the law because their interests in the land often would not be transferrable. Here, Lender conveyed Lot 7 to Phil through a proper non-judicial foreclosure sale. Because Phil acquired the property from a bona fide purchaser, who had the right to convey the property, he is protected by the shelter rule and acquired title superior to Bea.

(2) Lender does not have to reimburse Phil for payment made to discharge the federal tax lien. When a party forecloses on a property, the foreclosure sale discharges all interests junior to that of the foreclosing party so long as the holders of the junior interest were made parties to the foreclosure action. Certain types of liens, including federal tax liens, are not dischargeable even when a junior interest, however. The purchaser of the foreclosed property takes subject to the nondischargeable junior interests and to any interests more senior than the foreclosing party's interest in the property. Thus, the federal tax lien

remained on the property after the sale even though the lien attached to the property after the deed of trust by Lender was properly recorded and attached. But Phil took the property subject to that lien, just as he would have taken subject to any more senior liens on the property. The seller in a foreclosure sale makes only a quitclaim deed rather than a general warranty deed for precisely this reason. The seller knows it often cannot make the covenant that the property is free of encumbrances, and this is one reason why property sells so cheaply at most foreclosure sales. The deed from Trustee to lender does not change this result. That deed stated Terry and Terry's successors made the full warranty deed promises to Phil. It did not say Lender did so.

**END OF EXAM**