

President’s Mid-Year Message

By **Jeffrey E. Margolies, Esq., CLTP**
President, Maryland Land Title Association



It’s hard to believe that I’m already more than halfway through my tenure as President of the Maryland Land Title Association. Quite frankly, I’m proud of all the accomplishments that our Committees have made to date. I am pleased to provide you with the following Report.

ALTA PRINCIPLES OF FAIR CONDUCT

At our December Board Meeting, the MLTA adopted the *ALTA Principles of Fair Conduct*.

The *ALTA Principles of Fair Conduct* represent our commitment to promote behavior within the title industry that serves the needs and interests of consumers. The Principles describe ALTA’s, and our, expectation of our members to adhere to the highest standards of ethical behavior and the laws and regulations governing the business of title insurance. Please visit the link on our website to review the “Appropriate Steps to Implement the ALTA Principles”, which sets out specific actions that members can take, and suggests what government can do to assist the title industry in this regard. We encourage all of our members to pledge to support The Principles, and to incorporate them into their daily business practices. In turn, the MLTA pledges to assist our members in implementing The Principles through ongoing training on ethical standards and legal compliance.

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Maryland Foreclosures: Reformed

By **Martin Goldberg, Esq.**

On April 3, 2008, Maryland’s Governor enacted emergency legislation (House Bill 365, Senate Bill 216) restructuring Maryland’s mortgage foreclosure laws. The majority of mortgage foreclosures will now be conducted by a procedure one step shy of a purely judicial foreclosure proceeding, but with all the functional trappings of a litigation. The legislation features new content requirements for certain deeds of trust and mortgages, pre-foreclosure filing notice requirements, and personal service of the foreclosure complaint and consumer protection notice/disclosure in an effort to afford mortgagors and property owners greater notice of a foreclosure. The legislation became effective when enacted, and will be codified under Maryland Annotated Code Real Property Article, sections 3-104.1 and 7-105.

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Common Pitfalls to Avoid in 1031 Exchanges

By Marie C. Flavin

Section 1031 of the Internal Revenue Code allows investors to defer the capital gain tax normally due on the sale of investment or business use property by exchanging into other like kind investment or business use property. This section of the tax code is extremely beneficial to real estate investors because it allows them to reinvest all of their net equity into another investment property without paying capital gain taxes. Because of the tremendous tax savings benefits under Section 1031, exchanges are very commonplace in today's real estate market. However, there are many pitfalls to avoid under Section 1031 of the Internal Revenue Code and the 1031 IRS Treasury Regulations. Investors can find themselves facing a hefty tax bill if their exchange is not structured properly. This article will discuss some of the more common pitfalls and mistakes made by investors, real estate agents, or advisors.

Pitfall Number 1 Investors fail to obtain "replacement" debt.

Most investors understand that they need to reinvest the net proceeds realized from the sale of their relinquished property into like kind replacement property. Many fail to realize that they must also replace the debt they were relieved of when the relinquished property was transferred to a buyer. For example, if an investor sells a property for \$100,000 with debt in the amount of \$75,000, they must not only reinvest the \$25,000 of equity, but they must also acquire replacement property with at least \$75,000 of debt. They can take on more debt if necessary to acquire a higher value replacement property as long as all of the net equity is reinvested. Additionally, an investor can always add additional cash out of pocket towards the purchase of replacement property. On the other hand, if an investor only reinvests the net equity without replacing their debt, the IRS will tax them on the "debt relief" they experienced when their relinquished property was sold to a buyer, and the debt on the relinquished property was paid off or assumed. An investor who thinks that he has a

perfect exchange because he spent all of the cash towards the purchase of new investment property is quite upset when he learns that his transaction is taxable (sometimes 100% taxable in instances when the gain is quite large) simply because he was misinformed and did not know that he needed to obtain replacement debt.

[1031s Continued on Page 13.](#)

MLTA COMING ATTRACTIONS

Title Cruise

9 am to 4 pm

July 15, 2008.

Approved for 4 hours of CE credit.
Lunch will be served. Spouses/Guests are invited. No Children! Tickets are \$90 each. (Nonmember CE tickets are \$175).
At the end of the CE session, from 3 to 4 pm, we will hold a **cocktail hour**, serving wine and beer.

First Annual Crab Feast

Meet the MLTA Board of Directors

July 23, 2008

4 to 8 pm

The cost is \$35.

This event is a business social function. Spouses/guests are invited. However, all attendees, regardless of age, must purchase a ticket for \$35 each.

MLTA 2008 Fall Convention

September 11 to 14, 2008

Clarion Resort - Ocean City, MD
Reservations - Call 800-638-2100. Tell them that you are with MLTA.

Bull & Oyster Roast

November 8, 2008

at "Putting on the Ritz" in Columbia.

Upcoming Ideas...

A *Golf Tournament* is in the planning stages for October. Be on the lookout for additional information.

Foreclosures continued from page 1...

As background, for many years, Maryland's foreclosure process has been an *ex parte, in rem* summary proceeding, whereby from the date a foreclosure is filed with the Circuit Court, a Trustee exercising a power of sale could conduct a foreclosure sale fifteen days from the date suit was filed with the Circuit Court, provided the sale was properly advertised in a newspaper of general circulation in the county where the property is situate, and notice of the sale is sent to the mortgagor and other interested parties no more than thirty and no less than ten days prior to the sale by first class mail and by certified mail, return receipt requested. The summary nature of the procedure has historically allowed lenders to expeditiously recover collateral in times of economic strife, when borrowers were less able to repay their debts or restructure defaults, and the secured collateral was declining in value. Maryland's new law generally suffers lenders seeking to foreclose mortgages secured by residential property with an extended foreclosure process during periods of beleaguered housing markets marred by rising loan delinquencies and devaluing collateral.

First, the law defines "Residential Property" as property improved by "four or fewer single family dwelling units". It mandates that every mortgage or deed of trust secured by residential property recorded after the enactment date must contain the name and license number of the mortgage originator and mortgage lender, or, an affidavit certifying the originator and/or lender is exempt from the licensing requirement, Maryland Annotated Code, Real Property Article, section 3-104.1. Shortly after enactment, the Commissioner of Financial Regulation issued an advisory (posted on the Department of Labor, Licensing and Regulation's web site at:

<http://www.dllr.state.md.us/finance/advisories/advisoryapril72008.htm>) stating that the Commissioner is drafting regulations to address the issue, and until the regulations are implemented, mortgages and deeds of trust lacking the required information will be accepted for recording in land record offices without penalty to the lender.

Whether a loan has a commercial or consumer purpose has no bearing in determining whether the

foreclosure must comport with the new law. If mortgage collateral qualifies as "residential property", the foreclosure must proceed under the newly enacted statute. The term "single family dwelling units" is not defined. The intent of the legislation was to address the foreclosure of single-family residences serving as mortgage collateral. Clearly, purely commercial property is exempt from the new process, but the foreclosure of mixed use property and multi-family rental investment property containing four or fewer 'single family dwelling units' is ensnared by the undefined term.



Uniform mortgage instruments employed in the residential mortgage industry contain breach provisions whereby on default, a lender must send a borrower a thirty day notice to cure the delinquency. Most defaults are predicated on a failure to pay regular monthly mortgage payments. As a matter of industry practice, the demand notice is usually sent once a loan is two or more months delinquent. On issuance, lenders attempt to contact the borrower to engage in loss mitigation by repayment plan, loan modification, or other similar technique. If the borrower does not cure the default, or loss mitigation attempts fail, the lender is compelled to either commence a foreclosure or continue suffering monthly losses.

Now, under Maryland's reformed foreclosure process, in addition to a breach letter, to foreclose a mortgage secured by residential property, a forty-five day Notice of Intent to Foreclose must be issued by first class mail and certified mail, return receipt requested, to the mortgagor *and* record property owner. A copy also must be sent to the Commissioner of Financial Regulation. A sample form notice can be found on the Commissioner of Financial Regulation's web site, and is codified under COMAR 09.03.11.01. The form must contain

the name and telephone number of the secured party, mortgage servicer (if applicable), and an agent of the secured party who is authorized to modify the terms of the loan; the name and license number of the Maryland mortgage lender and mortgage originator (if applicable); the amount required to cure the default and reinstate the loan, including all past due payments, penalties, and fees; and any other information that the Commissioner of Financial Regulation requires by regulation.

The aforementioned advisory issued by the Commissioner also addresses situations in which the mortgage originator name or license number or lender license number cannot be identified for inclusion in the Notice of Intent to Foreclose. Under certain circumstances, if this information cannot be obtained from the face of the subject mortgage and/or after telephone inquiry with the Commissioner's office or via the Commissioner's on-line database, the failure to include the information is excused.

There are four instances in which a lender can petition the Circuit Court for leave to immediately foreclose absent issuance of a Notice of Intent to Foreclose. The mortgagee must prove that the loan was procured by the borrower's fraud or deception, the mortgagor has never made a payment on the loan, the secured property has been "destroyed", or "the default occurred after the stay has been lifted in a bankruptcy proceeding". Notably absent are circumstances in which property is vacant and abandoned, constitutes a public nuisance, or is suffering partial yet substantial waste.

Once the forty-five day Notice of Intent to Foreclose expires, **and**, the loan is at least ninety days in default, a foreclosure action can be filed with the Circuit Court. Under the former law, an Order to Docket Suit was filed, supported by the original or a certified copy of the mortgage or deed of trust, the original or certified copy of the debt instrument, *i.e.*, promissory note, a statement of mortgage debt, and an affidavit regarding the mortgagor's military status. Now, an Order to Docket Suit must also be supported by additional information and documentation, *i.e.*, the license numbers of the mortgage originator and mortgage lender must be identified (just as the

Commissioner's advisory addresses the mortgage and lender information requirements for the Notice of Intent to Foreclose, it similarly treats them for Orders to Docket Suit), an affidavit stating the nature and date of the default, an affidavit that the notice of intent to foreclose was issued in conformance with the law, a copy of the Notice of Intent to Foreclose, an affidavit certifying ownership of the debt instrument, the original or a certified copy of the deed of appointment of substitute trustee or assignment of mortgage for foreclosure, and a statutorily proscribed consumer protection notice to the mortgagor warning that a foreclosure has been filed, that a sale can be held forty-five days from the date the complaint is served, and that the mortgagor has legal options, including the right to seek injunctive relief and petition for bankruptcy, and that the mortgagor may want to seek the advice of a lawyer, real estate broker, or non-profit foreclosure counseling organization approved by the State of Maryland.

Once docketed, a copy of the Order to Docket Suit and all supporting exhibits, affidavits, and the consumer protection disclosure must be personally served on each mortgagor (or left with an individual of suitable age at the mortgagor's 'dwelling house or usual place of abode'). If two good faith attempts at service on two different dates prove unsuccessful, an affidavit detailing the attempts must be filed with the Court and the documents can be posted on the collateral residential property in a conspicuous place and sent to the mortgagor's last known mailing address by first class mail and certified mail, return receipt requested. Once alternatively served, proof of service must be filed with the Court and a sale can then be conducted no earlier than forty-five days from the date of service. What constitutes the date of service in the alternate service context is uncertain and open to interpretation.

There are a few items the new law does not impose or change. Specifically, it does not mandate the issuance of a summons, afford the mortgagor an opportunity to file a formal responsive pleading to the complaint on service, or require entry of a judgment or decree before a sale can be conducted. It does not amend notice of sale requirements regarding the actual sale, the parties to whom

notices must be sent and the manner of transmission (functionally giving the mortgagor upwards of four pre-sale notices during the process). Nor does it alter judicial processes for ratification of the sale and ratification of the Court Auditor's post-sale financial audit of the sale. The order of ratification of the sale retains its preclusive effect as to the fairness and propriety of the proceeding but the legislation does afford parties up to three years from the date the Court ratifies a sale to bring an action for failure to comply with the statute.

Finally, the law provides that on the mortgagor's request for reinstatement figures to cure a default, the mortgagee must provide the amount due and instructions for delivering funds within a reasonable period of time. Further, contrary to the terms of most uniform mortgage instruments, mortgagors now have the statutory right to cure financial defaults up to one business day before the actual foreclosure sale.

Given the additional and substantial new requirements imposed by Maryland's foreclosure reform act, foreclosure trustees, Circuit Courts, and title practitioners will need to exercise great care to respectively ensure process compliance when prosecuting foreclosure actions, reviewing reported sales for ratification, and ensuring title derived from a mortgage foreclosure is good and marketable.

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For more information about MLTA and the benefits of membership, please visit

www.MDLTA.ORG

Second Chapter in the Life of MLTA

By Eric Schneider, Past President

A number of years ago, the Board of Directors of the MLTA found itself grappling with two issues: first, what additional membership benefits could we offer to encourage new members to join the Association, and second, how could we improve the flow of information from each of the Counties (and Baltimore City) to the rest of the state. The Board (with substantial input from Jan Lynch) acknowledged that both issues could be addressed with a single solution – the “Chapter” concept.

In its original incarnation, the MLTA envisioned creating 24 separate Chapters – one for each jurisdiction in Maryland. The Chapter would become a local town meeting where members from each of the various Counties could meet and discuss what was going on in their jurisdiction. This could range from practice and procedure, to new regulations, recording or taxation issues, to professional networking. Soon the Board realized that organizing such a large number of sub-associations would be unwieldy, so they scaled back the concept: How about Regional Chapters?

The Board turned to Jan Lynch and Ted Rogers to organize the first MLTA Regional Chapter in the Southern Maryland region (to include Calvert, Charles, Prince George's, and St. Mary's Counties). The successes of this Chapter have been chronicled by its first Chair, Connie Fuksa, in the last two issues of this newsletter. Because Connie has been so successful in growing the first MLTA Chapter, the Board of Directors determined that it was time to begin our second Chapter.

Metro-DC Chapter Continued on page 7.

WHO WILL GUARD THE GUARD...?

By Michael Tracy

Employee dishonesty is a very real and potentially crippling exposure in the title industry. Most employees are trustworthy; a very few are not. Fidelity Bonds and Insurance are designed to protect business owners from the consequences of dishonest acts (essentially embezzlement by employees).

Some Observations

It is estimated that in the last four years, the average residential title agent in the Mid-Atlantic region had between 4 and 4.5 million dollars in his escrow account at any given time. That can be very tempting to an unscrupulous employee looking for an opportunity. A title agency owner functions in many different roles; in marketing and underwriting, as attorney, accountant, closer, and Human Resources expert.. and so on and so on. Either the owner has the talents (and time) to fill all of these roles, or he hires personnel with the necessary skill set to help conduct his business. He depends on competent and ethical staff support.

Until recently, the industry has enjoyed great profitability, but now the consequences of the hectic pace of that period are beginning to surface - as in, mistakes made (E&O coverage) and employee fraud losses (Fidelity coverage) - at the same time that profit margins are diminishing. Lax monitoring of controls, both in underwriting and accounting, during that period are the main causes of the problem. Fidelity losses seldom make the front pages of the *Baltimore Sun*, the *Philadelphia Enquirer*, *Washington Post*, or *Richmond Times-Dispatch* for several reasons. Title agents may be too embarrassed and fear the negative reflection on their client trust relationships and management skills. Underwriters would prefer neither to embarrass the agency nor to acknowledge that the loss occurred on their watch/audits.

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[Metro-DC Chapter from page 6...](#)

Realizing that yours truly was now the immediate Past President of the Association and therefore must have a lot of time on his hands, the Board asked me to help begin work on this next Chapter. We have decided that the Second Chapter of the MLTA will be entitled the Metro-DC Chapter and will pull from members who work in Frederick, western Howard, Montgomery, and northern Prince George's Counties, as well as the District of Columbia. As with the successful Southern Chapter, we hope to bring together MLTA members in a professional setting (*i.e.*, collection and dissemination of information, local educational programs, *etc.*), as well as social functions. If we are half as successful as Connie has been in Southern Maryland, the Board would be thrilled.

How do we get a Chapter started? We have scheduled an organizational meeting for
**Thursday, July 10, at 8:30 am
in Rockville**

– coffee and a light breakfast to be served. MLTA members who are located in the proposed region have already been notified by email, so this may be a second notice to many of you who would be interested in becoming involved. We are hopeful that Connie Fuksa will be available to attend, as well to share with us what has (and has not) been successful in the Southern Maryland Chapter. We look forward to a good turnout of interested members, and I hope to report the results of a successful meeting in the next MLTA newsletter.



Eric Schneider is the Immediate Past President of the MLTA and is Maryland Counsel for Conestoga Title Insurance Company in Potomac, MD.

Sources of Fidelity Losses

The “hit and run” or “bust-out” losses, while they do happen, are rare. The reality is that most fidelity losses occur over a period of time and are a betrayal committed by a tenured and trusted employee. They generally involved a combination of forged and/or raised disbursement/payroll checks, kiting of operating/escrow accounts, “dummy” or dormant accounts, and the surreptitious movement of funds between them. Sometimes, collusion (inside and outside of the agency) is involved.

Last year, a seemingly innocuous discrepancy found in an underwriter audit, mushroomed into a well-concealed \$1,000,000 fidelity loss for a Maryland agent. In this matter, two factors were particularly disturbing: 1) the first forged check was written to pay off the culprit’s prior employer for an earlier act of embezzlement; and, 2) two months after this claim discovery, the same person applied for a key position with another large agency!! Fortunately, due to the prompt actions of the agency owner and his underwriter, the agency recovered the loss in full, and the offender is currently incarcerated.

The National Association of Insurance Commissioners (NAIC) and ALTA have circulated a recommended regimen of internal controls/procedures to help curtail losses. It would be prudent to obtain a copy and heed its proposals. The use of electronic processing, with built-in security disciplines and cross-checks, has also helped reduce exposure to fidelity losses. A key concern: is your CPA well-versed in title escrow accounting?

If You Discover a Loss

- Immediately call your underwriter, who can be of valuable assistance in getting the salvage or recovery effort underway. Time is of the essence.
- Report the alleged theft to the police.
- Report the claim to your fidelity insure
- If forgery of checks was involved, put your bank on notice.

If the alleged culprit has a drug or “track” habit, don’t expect full recovery. Conversely, if he/she has area roots - family, financial interests, *etc.* - salvage may be much more likely. . . the stolen funds may be spent, but not necessarily squandered. Real estate and other attachable assets present an avenue to recovery. An astute title agent or underwriter can perform an asset search and obtain deeds of trust and/or confessed judgment notes to secure title to fraudulently acquired assets. Simple repayment notes often “go the way of the wind” with the passage of time. When hiring key people, consider paying a professional security firm \$300 to \$500 to conduct an extensive background investigation on applicants. In the long run, it could save big money and big headaches. Can you afford it? Can you afford not to?

Again, Who’s Going to Guard the Guard?

You, as agency owners, have the right and obligation to protect yourselves, your clients, your underwriter, and your employees, among other interested parties. The staff needs to accept and appreciate an owner’s (as well as an underwriter’s) duty to “open the window and look inside” from time to time. Sound internal controls require this course of action. Make sure the window is not locked or beclouded.

Underwriters’ audits have proven to be a valuable tool in detecting and limiting losses from a variety of causes. The audit often can act to deter those employees considering an embezzlement scheme, as such an audit is likely to expose any fraudulent activity.

But you, the owner, are responsible for implementing sound internal processes, accounting controls, cross-checks, and monitoring that will remove the bars from the windows. **YOU ARE THE GUARD GUARDING THE GUARD!!!**

Michael Tracy is an executive at the Chesapeake Insurance Group located in Annapolis, MD.

LEGISLATIVE COMMITTEE

We are fortunate that **Jim Cosgrove** (Chair of the Legislative Committee) and **Bill Pitcher** (our lobbyist) were actively monitoring proposed legislation and sending out notices to our membership. Their hard work, and dedication, kept us all up-to-date with the most recent actions on the Hill.

To fully understand and appreciate all the work that Jim (and the Legislative Committee) does on our behalf would require an inordinate amount of hours watching him reading and dissecting pages upon pages of legislation. How Jim is able to juggle his time chairing the Legislative Committee and managing an office of a title agency is beyond me.

This year, in particular, brought upon much legislation that directly impacts our industry, including the Task Force to Study the Title Industry. We all knew that when the Task Force was presented, it was going to be created. The original, proposed Task Force was made up of many sectors of the real estate industry, including a lopsided number bankers to title professionals (6 bankers/3 title professionals). With Jim's and Bill's efforts, we convinced the Legislature to change the committee make-up to include only 3 bankers.

The Legislative Committee is also focused on SB 216, 217 and 218 and how our industry can be an active participant in the new regulations being promulgated by DLLR, including how the new regulations relate to placement of mortgage lender/broker license numbers on security instruments, how recordation of security instruments may be affected by failure to place licensee information (or an affidavit in lieu thereof) on security instruments, and the new foreclosure rules.

Look to your e-mails for our forthcoming Legislative Report.

On the national level, our ALTA Liaison, **Sally McCash**, has kept us informed of Federal Legislation, including the new proposed RESPA reform legislation. Most recently, Sally has sent the membership an e-mail that "we have won the battle to get more time to make comments on the proposed RESPA reform legislation". I urge each of you to carefully review Sally's most recent message to membership, and act accordingly.

CERTIFIED LAND TITLE PROFESSIONAL DESIGNATION

Michael Schleupner and **Stuart Resnick** have revamped the Certified Land Title Professional (CLTP) program to make the designation more respected within

our industry. The CLTP designation has been updated to reflect not only accomplishments within the industry, but also industry knowledge and experience. In addition to some changes in the "point system", the roadmap for the CLTP designation now includes an Exam and Interview. The revised program, which can be found on our website, will help solidify our mission to promote professionalism throughout the industry.

CONVENTION COMMITTEE

Howdy Partner – *Boots on the Beach...* **Jeanne Shawahin** and **Ruth Kohl**, Co-Chairs of the Convention Committee, are well on their way preparing an outstanding Convention in *Ocean City Maryland*, which is scheduled to take place from *September 11-14, 2008*, at the Clarion Resort, Fontainebleau.

I am very excited about the program, the new "creative" educational offerings, and the other activities that the Convention and Education Committees are working on to make this Convention one not to be missed!

Mark your calendars and book your rooms, NOW, before they are sold-out.

Further information will follow on the website and future mailings.

Another goal for the Board and Convention Committee was to plan-ahead. Accordingly, Convention locations for the next few years have been adopted by the Board, as follows:

- 2009 Convention Ocean City, MD
- 2010 Convention Ocean City, MD
- 2011 Convention Williamsburg, VA

EDUCATION COMMITTEE

A big WOW to **Nancy Gusman** and the Education Committee. Since October, we have had numerous regular Continuing Education events, each in a different County.

Additionally, we have held several successful "Nuts & Bolts" programs, at Turf Valley Country Club, and will continue to offer the sessions there and at the Comfort Inn in Bowie.

Our annual *Title Cruise*, a mix of an educational/social event, is scheduled for *July 15, 2008*.

We are also planning 8 hours of continuing education at the Convention in September.

Who could ask for more? We've had more educational offerings than we have ever had in the past!

With our “look-ahead” objective, the Committee is already working on next year’s schedule, with a different topic being taught in different counties throughout Maryland. Title Cruise is planned to again be held in 2009, and there is a new plan to rotate the location for “Nuts & Bolts” between the Turf Valley Country Club (in Ellicott City) and the Comfort Inn (in Bowie).

We also are working on adding Saturday classes, once every quarter.

You can view the upcoming schedule (which is constantly being updated) at our Website.

PRE-LICENSING

MLTA workaholic, **John Gilbert** (and the Pre-Licensing Committee) continues to revamp, modify, and update our title insurance pre-licensing course to assist the title insurance producer/title insurance producer independent contractor candidate in passing the Maryland Insurance Administration’s new 100 question title licensing examination. This course is offered several times throughout the year.

Our next class is in August. This year’s schedule
August 13th and 18th, 2008
October 1st and 6th, 2008
December 3rd and 8th, 2008

MIA LIAISON COMMITTEE

Tom Gibbons has been very active in keeping open the lines of communication between the MLTA and the Maryland Insurance Administration (the “MIA”). In addition to the Liaison Committee’s recent meeting with the MIA, Tom is now in the process of scheduling a “meet and greet” with not only the members of the MIA, but also the Insurance Commissioner and several key personnel with the DLLR (Division of Licensing and Regulation). This is extremely important, as we want to make sure that the MIA and DLLR can trust and rely upon us for valuable input before they introduce legislation that impacts our industry and the consumer.

MEMBERSHIP COMMITTEE

Tobie Jacobs has been working to provide more benefits for our members. Her accomplishments include:

- Providing support for the new MLTA Chapters
- Guiding the new TIPIC sub-committee
- Balancing the needs of the TIPICs, our agents, underwriters and affiliated business members

- A NEW EVENT for the MLTA... our *first Crab Feast*, which is scheduled for *July 23, 2008* at “Centennial Park Pavilion D” in Ellicott City. *Tickets (\$35 each) can be purchased, NOW, on-line or from any of our Board Members.*
- ANOTHER NEW EVENT for the MLTA... Our first *Bull & Oyster Roast*, which is scheduled for *November 8, 2008* at “Putting on the Ritz” in Columbia. You won’t want to miss this event. *MARK YOUR CALENDARS NOW!!!*
- A Health Insurance Offering (information to follow)

TIPIC SUBCOMMITTEE

The Board recognized that further inclusion and understanding of the needs of the Title Insurance Producer Independent Contractors (TIPIC) was essential to the health and growth of the MLTA. To help us achieve this goal, we established a TIPIC subcommittee to specifically address the needs and concerns of our newest influx of members. This sub-committee, led by **Ganiyu Raji**, under the guidance of Tobie Jacobs, held its first meeting on November 7, 2007, and has met monthly since then. By opening up a better line of communication with our TIPIC members, we have met many of our goals, including:

- Improved communication with membership
- Professional development through education, and
- Helping our TIPIC members with their business development by incorporating them as committee members and encouraging them to enhance their skills by attending frequent educational offering and other MLTA networking events

Through a survey that was sent to our TIPIC members, the TIPIC subcommittee was also instrumental in providing additional ideas, including:

- Clarifying job postings and want ads on our Website
- Exploring options for Saturday continuing education classes
- Exploring rotation for continuing education classes
- Enhancing the membership roster on our website

SOUTHERN MARYLAND CHAPTER (and FUTURE CHAPTERS)

Special thanks go to **Janice Lynch** for spearheading the development of our first Chapter of the MLTA... the Southern Maryland Chapter.

This Chapter, which is now chaired by **Connie Fuksa**, successfully coordinated an educational offering in Charles County, in conjunction with a cocktail party that was attended by over 100 of our members. The Southern Maryland Chapter is now in the process of coordinating individuals to join/assist our standing committees in bringing pertinent information between the Southern Maryland region and the MLTA. They are also meeting with the local Clerks of Court to establish liaisons with the county government(s).

Connie has also agreed to assist **Eric Schneider** in formulating our next Chapter... the Suburban Maryland Chapter. I'm confident Eric will be just as successful as Connie in our newest endeavor.

NEWSLETTER

Kristopher Sleeth "stepped up to the plate" and gave us a new, improved and exciting look for the MLTA Newsletter.

He has done an excellent job at taking our Newsletter to the next level.

WEBSITE

Our website has undergone a complete overhaul, including an online Calendar of Events, active links to the ALTA website, a member-interactive sign-in that will allow you to make changes to your membership information "on the fly", and a fresh "new" look.

Additionally, access to Board Meeting minutes, and other documentation, can now be accessed through our members-only password-protected section.

Special thanks to **Jeffrey Thompson** and **John Shepherd** (our Webmaster) for revamping our website.

Please visit our new and improved website at <http://www.mdlta.org>. As this is a continuing work in progress, if anyone has any ideas, please feel free to contact Jeff.

CHARITABLE CONTRIBUTIONS

The MLTA has always been a strong advocate of "Giving Back to our Community." A few years ago, we

endowed the Maryland Land Title Association Foundation. As noted in the Foundation's website (www.mltafoundation.com), the Foundation was approved by the IRS in February of 2006, as a 501(c) (3) Organization. The MLTA Foundation seeks to:

- Enhance and preserve the integrity of land titles,
- Promote the recognition of current and historic contributions of land title professionals in our community,
- Recognize and promote excellence and quality in the industry and its supporting institutions, and
- Support preservation of historic buildings.

The Foundation's website also notes that it: "works to provide an effective means for the conveyancing industry to come together to engage in related charity and philanthropy, strengthening the industry by providing its members with the opportunity to give back in a way that is uniquely important and rewarding to them. It seeks to build and manage a permanent endowment to meet local industry member needs, make contributions to other non-profit organizations, provide community leadership including leveraging resources and conveying organizations to solve problems, and provide a central philanthropic vehicle for donors to meet their needs."

I urge you to consider making a contribution to the Foundation.

We have also made several other charitable contributions, throughout the years.

A brief summary of our donations over the past few years is available to members, upon request.

As I've noted several times in the past, the MLTA would not be what it is, today, without the dedication of its Officers, Directors, Committee Chairs, Committee Members, and our Executive Director, **Margaret Webb**. We could not have accomplished so much, in so short a period of time, without the vast amount of time and effort which they have devoted to our organization.

If you wish to contact any of our officers, directors and/or committee chairs, their contact information can be found at our website: www.mdlta.org.

Thank you.

Jeffrey E. Margolies, Esq., CLTP
President, Maryland Land Title Association



**MLTA 2008 Fall Convention
September 11 to 14, 2008**

"Boots on the Beach"

**Ocean City, MD at the
Clarion Resort Fontainebleau Hotel**

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Call **800-638-2100** to make your
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***You must mention that you are with MLTA, or
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John Gilbert, Esq. CLTP - Prelicensing Committee
Commonwealth / LandAmerica

Jeff Thompson, Esq. CLTP -Technology Committee
Chicago Title Insurance Co.

put down the wrong street address or lot number; they leave off the city and state; they fail to note that they are buying only a percentage of the property; they fail to include any improvements that will be constructed to the property before it will be acquired; they squeeze six properties onto the three lines (there are limits as to how many properties can be identified); *etc.*

Unfortunately, what would appear to be a minor procedural requirement has major implications for the exchange. After midnight of the 45th day, there is no way to correct these errors. Taxpayers can be charged with tax fraud for backdating identification statements or otherwise trying to make it appear as if they properly identified their properties in a timely manner.

Pitfall Number 3

Investors believe that an exchange is an “all-or-nothing” tax benefit.

For example, assume an investor is selling a rental house in the city for \$200,000, and has found a rental house in a resort location valued at \$175,000. Sometimes, “partial” exchanges can be beneficial. This can be a partially tax deferred exchange, and they will owe capital gain taxes on the \$25,000 differential. Still, depending on the gain realized from the transfer of the relinquished property, there may still be some tax-deferral from the reinvestment into a smaller property. Investors should always consult with their tax advisors early on in the process to determine what their tax liability will be if they do not exchange, and how much replacement property they must acquire in the exchange to receive any tax benefit.

Pitfall Number 4

Investors think that exchanges only work if they are swapping properties with someone else.

Historically, all exchanges were structured as two-party “swaps” or trades. For example, assume Joe Investor owned a property in the city and Fred Farmer owned a property in the country. Joe wanted Fred’s property and vice versa. Joe and Fred swapped deed,s and each deferred payment of their capital gain taxes until such time that they liquidated their investment and received cash instead of like kind property.

The infamous *Starker* case changed history and the way exchanges were structured forever. In *Starker v. United*

*States*¹, the court ruled that there could be a delay between the time of the sale and the time of the purchase. Subsequent to the *Starker* case, the Internal Revenue Code was amended to include the strict time deadlines. Later, the IRS issued Treasury Regulations creating other acceptable exchange structures – including “Qualified Intermediaries.”

Today, Joe and Fred do not have to swap with one another. Joe can sell his property at the best price to Betty Buyer and, through the use of a Qualified Intermediary, purchase replacement property from Fred. Fred will sell to Joe; then, he can turn around and buy a better-priced property from Reasonable Ron. The use of a Qualified Intermediary today makes the entire exchange process simpler because an investor can essentially sell relinquished properties directly to buyers and buy replacement properties directly from different third party sellers.

Pitfall Number 5

Investors think they must trade a duplex for a duplex or land for land.

Under Section 1031, all real property is considered like kind with all other real property as long as the properties are held for either investment or business use. Exchangers can exchange out of a duplex and into any other real property that they intend to hold for investment purposes or for productive use in their trade or business. Residential rental properties are like kind to commercial buildings. Improved properties are like kind to raw land. Fractional interests (held as tenants in common) are like kind to owning a fee simple interest in property. Long term ground leases with 30 years or more left to run on the lease (including extensions) can be like kind to other real property interests.

Pitfall Number 6

Investors don’t hold their properties for investment or business use.

Although all real property is like kind with all real property (see Number 5, above), the properties in the exchange must be held either for investment or business use, which excludes properties held primarily for sale or for personal use. If an investor sells a rental house, buys a condo in Palm Springs, and quickly begins to use the Palm Springs condo for personal use (as a second or retirement home), the IRS might disallow the exchange for failure to have the appropriate “investment” intent. With proper planning, however, an investor can initially

¹ 602 F.2d 1341, 44 A.F.T.R.2d 79-5525, 79-2 USTC P 9541 (9th Cir. 1979).

hold the Palm Springs condo for investment purposes by renting it out for a period of at least one to two years, then later “convert” the condo to a property used for personal purposes. Similarly, assume an investor acquires an office building and wants to turn around and sell it right away for a higher price. If that investor attempts to structure the transaction as part of a tax deferred exchange and is audited by the IRS, the exchange might be disallowed if the IRS takes the position that the office building was held primarily for sale as opposed to investment purposes. Furthermore, that investor would have to pay taxes on the sale of the office building at ordinary income tax rates, because one must own a property longer than 12 months in order to receive capital gain tax treatment (which provides for lower tax rates).

**Pitfall Number 7
Investors don’t consult with a tax or legal advisor.**

Many investors avoid seeking the advice of a tax or legal advisor because of the additional cost and inconvenience of having yet another party involved in the transaction. However, this can actually end up costing the investor more money in the long run if a tax or legal advisor gets pulled into a transaction late in the game when the damage has already been done. A tax advisor also can help decide whether an exchange is necessary or appropriate. For example, what if the relinquished property has a small gain, or perhaps even a loss? In this scenario, there is rarely a need for an exchange. If the investor has losses in other business activities, this could eliminate the need for an exchange. Additionally, many issues come up throughout an exchange that could be resolved quickly and favorably with the assistance of an experienced legal advisor. For example, many times there are problems with obtaining a new loan because of specific lender requirements that can jeopardize the exchange (i.e., requiring that a single asset entity acquire the replacement property when a husband and wife together sold relinquished property). Many, if not most, issues can be resolved with the joint assistance of an experienced Qualified Intermediary and the investor’s own tax and/or legal advisor.

**Pitfall Number 8
Investors don’t understand the need for a Qualified Intermediary.**

One of the most basic requirements under Section 1031 of the Internal Revenue Code is that you must have an “exchange” of properties, meaning a reciprocal trade. As discussed above, historically this trade was established by having two parties directly swap properties with each other. Obviously this type of exchange is difficult to

structure because you have to line up two parties who want each other’s property. The IRS established the concept of a Qualified Intermediary in 1991 to simplify the process. The Qualified Intermediary trades properties with the investor by acquiring the relinquished property from the investor and transferring it to a buyer for cash, then acquiring the replacement property with the cash from a different seller and transferring it to the investor. The Qualified Intermediary typically will produce the necessary exchange documentation that must meet some very specific requirements under the Tax Code and IRS Regulations. Additionally, it is imperative that the Qualified Intermediary holds the cash or controls the cash (i.e., gives instructions to the closer to move the money to the escrow where the purchase is going to take place). A Qualified Intermediary is necessary even for simultaneous exchanges wherein the investor is closing on their relinquished property and replacement property at the same time, because the investor still must create a trade of properties between two parties (between the investor and the Qualified Intermediary).

However, investors should be careful in their selection of a Qualified Intermediary, because not all Qualified Intermediaries are alike. Qualified Intermediaries can vary greatly in their level of expertise and security (or lack thereof) of exchange funds. Unlike most service providers in the real estate community, Qualified Intermediaries are completely unregulated. The IRS only prohibits agents (real estate agents, accountants, attorneys, etc.) and parties or entities that are related to the taxpayer from acting as a Qualified Intermediary. There is no requirement for Qualified Intermediaries to have a license, a bond, insurance, conservative banking and investment procedures, or any continuing education or training. Because Qualified Intermediaries hold the investors’ funds, the careful investor will inquire into the level of expertise and security offered by a particular Qualified Intermediary. Unfortunately, there have been several recent incidents wherein Qualified Intermediaries lost significant sums of exchange clients’ funds in the stock market, employees of the Qualified Intermediary have stolen exchange funds, or the Qualified Intermediary has become bankrupt or insolvent. Many Qualified Intermediaries will offer insurance, bonds, and/or written third party guarantees for the safekeeping of exchange funds.

**Pitfall Number 9
Investors call the exchange company to set up an exchange AFTER closing on the sale of their relinquished property.**

As discussed in Number 8 above, the Internal Revenue Code Section 1031 requires that there be a reciprocal

trade of properties. If a sale transaction closes without a Qualified Intermediary and without the written exchange documentation in place and signed prior to closing, it is too late to put an exchange together and the transaction is taxable. This is the case regardless of the fact that the contract had a clause in it documenting the intent of the seller to effectuate a 1031 exchange or the fact that the funds have not been disbursed from escrow. One possible remedy is for the seller and buyer to rescind the transaction and put each other back into their original positions -- the seller gives the money back to the buyer and the buyer delivers a deed to the seller. A rescission is next to impossible if there is financing involved in the transaction. This miserable situation can be avoided by simply setting up the exchange with a Qualified Intermediary on or before the closing date.

**Pitfall Number 10
Investors miss a deadline.**

The strict time deadlines are probably the most difficult aspect of 1031 exchanges. The investor has 45 days from the date the relinquished property closes to identify potential replacement property, and 180 days (or the tax filing deadline, whichever comes sooner) in which to close on an identified property. These time deadlines are not extended for weekends, holidays, or good faith efforts by the taxpayer. If the investor decides to purchase a property that was not identified during the 45-day identification period, or if the investor is unable to close on the purchase of replacement property within the 180-day exchange period, the exchange fails and the capital gain taxes must be paid. Short of a “Presidentially declared emergency” (e.g., 9/11) the Treasury Department does not have the authority to extend the time deadlines. Therefore, the Qualified Intermediary companies most certainly cannot extend the time deadlines, no matter how accommodating they might be or how compelling a particular investor’s situation is.

In conclusion, there are many ways an investor can get tripped up in the tangles of complicated IRS rules and regulations and the tax code requirements of a 1031 exchange. With careful planning and an experienced team of professionals, including the tax advisor, legal advisor, real estate agent, title and escrow officers, loan officer, and the Qualified Intermediary, a tax deferred exchange can be properly structured and successfully closed. Investors also should always take an active role in their real estate and exchange transactions, and ask questions of their professionals along the way to ensure a smooth transaction without any tax or legal tangles.

Marie C. Flavin, Esq. is Vice President and the Northeast Regional Manager for Investment Property Exchange Services, Inc.

The MLTA is a professional organization working on behalf of title industry service providers and consumers. We hope that you will consider joining the many agents, abstractors, attorneys, and underwriters who already have benefited from their membership.

From the Editor:

In this issue, MLTA President Jeffrey Margolies touched on the MLTA’s adoption of the *ALTA Principles of Fair Conduct* and how these principles represent our commitment as title professionals to the best interests of our clients and the public. This is one reason we chose to adopt a new name for our quarterly publication, now called the *MLTA Commitment*. We also want this title to represent MLTA’s dedication to its membership.

The goal of the *Commitment* is to inform and educate its diverse membership. This requires *your* input. If you have any comments, ideas, or topics that you would like to see included in the *Commitment*, please pass them along.

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