



Know Your Entity:

How to Reduce Risks When Insuring Titles Granted by Corporations, Other Legal Entities, Trustees, and Churches

(Part Two)

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Limited Partnerships

A limited partnership is a partnership in which one or more partners, but not all of them, has no liability for the partnership's obligations. Unlike a general partnership, which may be created without any formal agreement or filing, a limited partnership may be formed only by filing a certificate of limited partnership with the SCC.³⁸ A limited partnership's existence normally commences on the filing of its limited partnership certificate; however, the certificate may provide for the limited partnership's existence at a later date.³⁹ A limited partnership may carry on any business that may be carried on by a general partnership.⁴⁰

Like a general partnership, a limited partnership may dissolve voluntarily. Unlike a general partnership, a limited partnership must dissolve involuntarily if the SCC cancels the limited partnership's certificate for failure to pay a required annual registration fee.⁴¹ Upon dissolution, a limited partnership must be wound up.⁴² A limited partnership's authority to transact business after dissolution is the same as a general partnership's. When a limited partnership has wound up its business after a dissolution, it is required to obtain a certificate of cancellation from the SCC.⁴³

Title insurers usually confirm a limited partnership's existence by obtaining a "certificate of fact" from the SCC. The certificate of fact should state that a certificate of limited partnership has been filed with the SCC and that the certificate has not been canceled.⁴⁴ If the certificate of fact indicates that the limited partnership's certificate has been canceled, then serious questions arise regarding the limited partnership's authority to sell or encumber real estate. Those situations should be referred to underwriting counsel.

After a title insurer verifies a limited partnership's existence the next step in the due diligence process is to review the limited partnership certificate and the limited partnership agreement to determine whether the transaction has been authorized. For all practical purposes, general partners in a limited partnership have the same power as general partners in a general partnership to manage a partnership's business.⁴⁵ Therefore, in determining whether a general partner is authorized to enter into a transaction on behalf of a limited partnership, title insurers should make the same inquiries as when dealing with a general partnership.

Although the Revised Limited Partnership Act does not specifically authorize a limited partnership to file

a statement of partnership authority, statement of denial or statement of dissociation with the SCC, the statute provides that cases not covered by the Uniform Limited Partnership Act.⁴⁶ This implies that the provisions of the Uniform Partnership Act governing statements of partnership authority, statements of denial and statements of dissociation apply not only to general partnerships but also to limited partnership authority; statements of denial and statements of dissociation apply not only to general partnerships but also to limited partnerships. This interpretation is not free from doubt because the Revised Uniform Limited Partnership Act provides that the filing of a certificate of limited partnership "is notice that the partnership is a limited partnership and that a person designated as a general partner is a general partner, but shall not be deemed to be notice of any other fact."⁴⁷ However, title insurers dealing with limited partnerships will probably wish to check the SCC's records regarding statements of partnership authority, statements of denial and statements of dissociation to the same extent as when dealing with general partnerships.

As mentioned above, only a general partner may execute legal documents on behalf of a limited partnership. However, limited partnership agreements sometimes require limited partners' consent for sales of financing transactions or for the disso-

lution and winding up of the limited partnership.⁴⁸ Therefore, title insurers should review a limited partnership's limited partnership agreement and its certificate of limited partnership to determine whether such consent is required. If so, the limited partners' consent must be obtained prior to closing.

When a foreign limited partnership sells or mortgages property, a title insurer should verify the foreign limited partnership's existence by obtaining a current certificate of fact from the limited partnership's state of organization. Although foreign limited partnerships that transact certain kinds of business in Virginia are required to obtain a certificate of authority from the SCC,⁴⁹ a foreign limited partnership's failure to qualify does not impair the effectiveness of the foreign limited partnership's deeds or mortgages of Virginia property.⁵⁰ To verify the foreign limited partnership's authority to own real estate and to determine whether a particular transaction has been authorized, title insurers should follow the same procedures as with a Virginia limited partnership.

Registered Limited Liability Partnerships

A general partnership or a limited partnership may register with the SCC as a registered limited liability partnership.⁵¹ The registration must be approved by the partners unanimously or in the manner provided in the partnership agreement for adopting an amendment to the agreement.⁵²

A partnership's registration as a registered limited liability partnership does not create a new legal entity;⁵³ instead, the registration simply limits a general partner's liability for future obligations of the partnership. Conversely, the voluntary or involuntary cancellation of a partnership's registration as a registered limited liability partnership does not terminate the partnership's existence.⁵⁴ To determine whether a registered limited liability partnership exists and whether it has authorized a transaction, title insurers should exercise the same due diligence as they do for general partnerships or limited partnerships.

Title insurers also should review any general partnership's statement of registration as a registered limited liability company. A general partnership's registration statement not only registers the partnership as a limited liability partnership. It also may serve as a statement of partnership authority, a statement of dissolution or a statement of dissociation.⁵⁵ Because these statements may affect a partner's authority to bind a partnership (see discussion above regarding general partnerships), title insurers should review these statements to make sure that a general partner who signs transaction documents is not exceeding his authority.

Finally, title insurers should review any voluntary cancellation statement filed with the SCC. A cancellation statement may contain a specific provision requiring the partnership's dissolution;⁵⁶ in that event, the partnership's authority to sell or mortgage property would be limited to transactions necessary to wind up the partnership's business.

Limited Liability Companies

A limited liability company (LLC) is created by one or more persons signing and filing Articles of Organization with the SCC.⁵⁷ An LLC's existence normally commences when the SCC issues a Certificate of Organization for the LLC; however, the LLC's Articles of Organization may provide for its existence to commence on a later date.⁵⁸ An LLC's owners are called "members," not shareholders or partners.⁵⁹

An LLC's existence is perpetual unless: 1) the Articles of Organization provide otherwise; 2) the members unanimously consent to dissolve; 3) a court of competent jurisdiction decrees the dissolution of the LLC;⁶⁰ or 4) the LLC's Certificate of Organization is canceled automatically for failure to pay annual registration fees.⁶¹ Automatic cancellation will occur if the LLC's annual registration fee remains unpaid as of December 31 following a notice of impending cancellation issued by the SCC based on the LLC's failure to pay its annual registration

fee on or before October 1 of the year assessed.⁶²

Title insurers may verify an LLC's existence by obtaining a recent "certificate of fact" from the SCC. The certificate of fact constitutes the SCC's official certification that a Virginia Limited Liability Company certificate has been filed in its office and that no certificate of cancellation has been filed. Because the Articles of Organization may provide for the LLC's existence to commence after the Certificate of Organization has been issued, title insurers should review the Articles of Organization to determine either that: 1) there is no provision for a deferred commencement date, or 2) that such date has arrived prior to the date on which the LLC acquired or will acquire the property to be covered by a title insurance policy.

If an LLC exists, it has the legal authority to own and encumber real estate, unless its Articles of Organization or any operating agreement provides otherwise. An operating agreement is an optional agreement by which the members of an LLC may provide for its governance. To protect against the risk of possible limitations on the LLC's authority to own or mortgage real estate, the title insurers should review the LLC's Certificate of Organization and any operating agreement.

Upon verification of an LLC's existence and its authority to own and mortgage real estate, title insurers should verify that the LLC has authorized the proposed sale or encumbrance of its property. An LLC has enormous flexibility to determine its own form of self-governance through its Articles of Organization or operating agreement.⁶³ Therefore, in reviewing these documents, title insurers should determine what internal actions the LLC needs to take in order to



buy, sell or mortgage property, and then require proof that the LLC has taken these actions. If neither the LLC's Articles of Organization nor its operating agreement provides for the purchase, sale, or mortgaging of property, then the LLC may make decisions on these matters by a vote of a simple majority of the membership interests, with members voting in proportion to their percentage of ownership in the LLC.⁶⁴

A common way to verify that an LLC has authored a real estate transaction is to obtain a resolution, signed by all of the LLC's members, approving the transaction. The resolution generally authorizes a "manage" or a particular member of the LLC to sign the transaction documents on its behalf. As when dealing with corporations, title insurers may also wish to obtain an incumbency certificate identifying the persons authorized to sign the transaction documents and providing exemplars of their signatures.

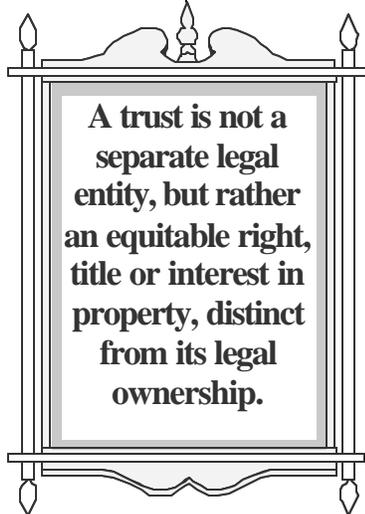
Although a resolution signed by all of an LLC's members provides the best protection against an unauthorized transaction, obtaining a membership resolution may be impractical in some cases – for example, if the LLC has numerous members, or if a manager has obtained the member's agreement (in the Articles of Organization or in an operating agreement) that the manager may sell or finance real estate without the consent or approval of the members. In such cases, title insurers may generally rely on actions taken in accordance with authorizations provided in the LLC's governance documents. However, in the absence of the unanimous consent of the members, title insurers should be alert for warning signs that a single member or manager lacks the necessary authority to sign legal documents for the LLC. Those warning signs are the same as the warning signs discussed

above in connection with partnership transactions.

The person executing any instrument affecting title on behalf of an LLC must be the person noted in the LLC resolution or, if no resolution is obtained, the person granted authority under the LLC's Articles of Organization or operating agreement.

When a foreign LLC sells or mortgages property, title insurers should verify the LLC's existence by obtaining a current certificate of fact from the LLC's state of organization. Although foreign LLCs that transact certain kinds of business in Virginia are required to obtain a certificate of authority from the SCC,⁶⁵ a foreign LLC's failure to qualify does not impair the effectiveness of the foreign LLC's deeds or mortgages of Virginia property.⁶⁶ To verify the foreign LLC's authority to own real estate and to determine whether a particular transaction has been authorized, title insurance professionals should follow the same procedures as with a Virginia LLC.

Trusts



A trust is not a separate legal entity, but rather an equitable right, title, or interest in property, distinct from its legal ownership.⁶⁷ It is a legal relation between two or more persons by virtue of which one, a trustee, is bound to hold legal title of property for the use or benefit of beneficiaries, who have an equitable title or interest in the property.⁶⁸

Generally, a person who deals with a trustee is on inquiry notice of the scope of the trustee's authority.⁶⁹ Therefore, if a trustee were to execute a deed or deed of trust without proper authority, the transaction would ordinarily be voidable by a beneficiary.

However, the Virginia Land Trust Statute provides a significant exception to the general rule: a person dealing with a trustee may rely conclusively on the powers recited in the deed by which the trustee acquired the land.⁷⁰ The statute provides that: "no person dealing with such a trustee shall be required to make further inquiry as to the right of such trustee to act, nor shall he be required to inquire as to the disposition of any proceeds."⁷¹

In dealing with a trustee, title insurers should carefully review the deed by which the trustee holds title. If that deed gives the trustee the power to deal with the property, the purchaser, lender or title insurance company may rely on that deed. No further inquiry is required concerning the trustee's authority to act or the application of the proceeds of a trustee's sale or financing of trust property. However, if the deed by which the trustee holds title does not give the trustee adequate power to deal with the property, title insurers should obtain a copy of the written trust instrument under which the trustee holds title to confirm that the trust instrument gives the trustee the power to deal with the property.⁷² In such cases, the instrument that the trustee signs to convey or encumber property should include recitals indicating that the trustee was acting within his authority under a specified trust agreement, accompanied by a citation to the specific provision of the trust instrument under which the trustee is acting. If a deed under which the trustee holds title does not contain the language necessary to bring the new deed or deed of trust within the scope of the Land Trust Statute, some attorneys attach a copy of the trust agreement to the trustee's deed or mortgage so that a title examiner may verify that the trust agreement authorized the trustee's actions.

Judicial approval of a transaction may be required if the terms of the trust instrument are silent or inconclusive as to the trustee's power to sell or mortgage property of the trust.⁷³

If a trust agreement has a specific termination date, the trust generally does not terminate on that date unless the trustee has disposed of all of the trust's assets.⁷⁴ However, a trustee's failure to wind up a trust by the specified termination date may be a warning sign to investigate whether the trustee has acted within his authority.

As always, title insurers should be alert to warning signs of misconduct. Self-dealing by a trustee is strictly prohibited,⁷⁵ so title insurers should never insure a transaction by which a trustee conveys property to himself or mortgages property for a purpose other than one of the purposes of the trust.

Churches

Unlike most states, Virginia prohibits churches or religious societies from incorporating.⁷⁶ By statute, title to church property generally must be held by trustees appointed for that purpose by the circuit court of the city or county in which the church's land is located.⁷⁷ However, whenever the laws, rules, or ecclesiastic polity of any church, religious society, or denomination so provide, a bishop or ecclesiastical officer of the church may hold title to the church's property.⁷⁸

The Virginia Code limits the amount of property that a church may own. The trustees for a church may not own, at any one time, more than fifteen acres of land in a city or town, nor more than 250 acres outside of a city or town and within the same county, unless authorized by an ordinance of such city or town council.⁷⁹ Although most churches are unlikely to own property in excess of these limits, a violation of the limits could cause a failure of title.

To sell or encumber any of the church's property, the church's trustees must file a petition with the circuit court of the county or the city wherein the land, or the greater part thereof, lies and obtain an order from the court authorizing the sale or encumbrance.⁸⁰ To obtain court ap-

proval of a proposed sale or encumbrance of a church's property, the trustees must prove that the sale or encumbrance "is the wish of the congregation, or church, or religious denomination or society, or branch or division thereof, or the constituted authorities thereof having jurisdiction in the premises, or of the governing body of any church diocese."⁸¹ A court order approving an encumbrance of a church's property may authorize the church's treasurer or other fiscal officer to sign a mortgage loan instrument without personal liability.⁸²

The evidence required to accompany the petition to the circuit court depends on the church's constitution or by laws. In independent congregational churches, the congregation must adopt a resolution authorizing the sale or encumbrance of the church's land. However, in the case of a super congregational church or a hierarchical church, a particular church's property is held in trust for the larger denomination, and the duly constituted authorities of the general church must approve the sale or encumbrance of the particular church's land. The various kinds of church organizations are discussed in detail in *Norfolk Presbytery v. Bollinger*, which held that a general church's claim to property used by a particular church should be decided



on the basis of the church's organizational structure and governance documents, without any inquiry into matters of religious doctrine.⁸³

To verify a church's authority to sell or encumber property, a title insurer must: 1) review the court order appointing the trustees or other offi-

cial to hold title to the church's property; 2) review the church's governance documents to determine what approvals are required for the sale or encumbrance; 3) review the congregational resolution or other approval to make sure that it authorizes the transaction in question and that it confirms to the requirements of the church's governance document; 4) review any approval granted by the general church or denomination, if the church's governance document require such approval; and 5) review the circuit court order authorizing the sale or encumbrance.

Conclusion

Transactions involving purchases or mortgagors that are legal entities involve off record risks not found in transactions where the only parties are individuals. Verifying an entity's existence, and the authority of the people acting on its behalf, requires due diligence in the form of obtaining applicable records from the SCC, the entity's governance documents and other appropriate materials, such as copies of corporate, partnership and limited liability company resolutions. By understanding the different kinds of legal entities and performing the due diligence required in each case, title insurance professionals can serve their customers and protect their underwriters by reducing the risks inherent in dealing with entities.

³⁸ VA. CODE ANN. §50-73.11 (Michie 1998). Compliance with the limited partnership act is the only way to create a limited partnership. *Pischke v. Murray*, 11 B.R. 913 (Bankr. E.D. Va. 1981); see generally *Oglesby Co. v. Lindsey*, 112 Va. 767, 72 S.E.672 (1911).

³⁹ §50-73.11(B).

⁴⁰ VA CODE ANN. §50-73.9 (Michie 1998).

⁴¹ VA CODE ANN. §50-73.69(B) (Michie 1998).

⁴² *Id.*

⁴³ VA CODE ANN. §50-73.13 (Michie 1998).

⁴⁴ A Certificate of fact from the Virginia State Corporation Commission will be signed by the Clerk of the Commission and will take the following form:

I Certify the Following from the Records of the Commission:

A Virginia Limited Partnership certificate was filed in this office on _____ by _____.

A certificate of cancellation has not been filed in this office by _____.

Nothing more is hereby certified.

⁴⁵ VA. Code Ann. §50-73.29(A) (Michie 1998) provides, in pertinent part, that "[e]xcept as provided in this Chapter or in the partnership agreement, a general partner of a limited partnership has the same rights and powers of a partner in a partnership without limited partners."

⁴⁶ VA. Code Ann. §50-73.75 (Michie 1998).

⁴⁷ VA. Code Ann. §50-73.19 (Michie 1998).

⁴⁸ VA. Code Ann. §50-73.24 (Michie 1998), governs a limited partner liable to third persons for a limited partnership's obligations. The general rule is that: "[A] limited partner is not liable for the obligations of a limited partnership unless he is also a general partner, or in addition to the exercise of his rights and powers as a limited partner, he participates in the control of the business." The statute provides that a limited partner does not participate in the control of the business by "[p]roposing, approving or disapproving, by voting or otherwise" various matters "which the partnership agreement states may be subject to the approval or disapproval of limited partners."

⁴⁹ VA. Code Ann. §50-73.54 (Michie 1998).

⁵⁰ VA. Code Ann. §50-73.59(B) (Michie 1998). See also VA. Code Ann. §50-73.61 (Michie 1998) (transactions not constituting doing business).

⁵¹ VA. Code Ann. §50-73.132 (Michie 1998) states the requirements for registering a general partnership as a registered limited liability partnership. VA. Code Ann. §50-73.61

⁵² VA. Code Ann. §50-73.132(C) (Michie 1998).

⁵³ VA. Code Ann. §50-73.137(E) (Michie 1998).

⁵⁴ VA. Code Ann. §50-73.137(B) (Michie 1998).

⁵⁵ VA. Code Ann. §50-73.136 (Michie 1998).

⁵⁶ *Id.*

⁵⁷ VA. Code Ann. §13.1-1010 (Michie 1999).

⁵⁸ VA. Code Ann. §13.1-1004(B) (Michie 1999).

⁵⁹ See generally, VA. Code Ann. §13.1-1038.1 (Michie 1999).

⁶⁰ VA. Code Ann. §13.1-1047 (Michie 1999).

⁶¹ VA. Code Ann. §13.1-1046 (Michie 1999).

⁶² VA. Code Ann. §13.1-1064.B (Michie 1998).

⁶³ An LLC's organizational documents may provide for the company to be managed by a manager or managers; otherwise, the members have the right to manage the LLC. The Articles of Organization and operating agreement may provide for the appointment of other officers and may allow officers to delegate their authority. See VA. Code Ann. §13.1-1022 (Michie 1999).

⁶⁴ *Id.*

⁶⁵ VA. Code Ann. §13.1-1052 (Michie 1999) (transactions not constituting doing business).

⁶⁶ VA. Code Ann. §13.1-1057.B (Michie 1999)

⁶⁷ Michie's JURISPRUDENCE, *Trusts and Trustees*, §2 (1991).

⁶⁸ See generally *Hancock v. Anderson*, 160 Va. 225, 168 S.E.458 (1933).

⁶⁹ *Utterback's Adm'r v. Cooper* 69 Va. (28 Gratt.) 233 (1877) (persons dealing with a fiduciary are charged with notice of extent of their authority).

⁷⁰ VA. Code Ann. §55-17.1 (Michie 1995) provides that a trust will not fail merely because it fails to specify the beneficiaries by name or specifically outline the trustee's duties. This section states:

No trust relating to real estate shall fail nor shall any use relating to real estate be defeated because no beneficiaries are specified by name in the recorded deed of conveyance to the trustee or because no duties are imposed upon the trustee. The power conferred by any such instrument on a trustee to sell, lease, encumber or otherwise dispose of property therein described shall be effective and no person dealing with such a trustee shall be required to make further inquiry as to the right of such trustee to act, or shall he be required to inquire as to the disposition of any proceeds.

⁷¹ *Id.*

⁷² *First Funding Corp. v. Birge*, 220 Va. 326, 333 (1979) ("A trustee under a deed of trust is authorized to act with reference to the trust property only in the manner which the deed either by express terms or by necessary implication provides."); See *Schmidt & Wilson v. Carneal*, 164 Va. 412, 415 (1935); *Wilson v. Wall*, 99 Va. 353, 355 (1901); see also *Tuscarora, Inc. v. B. V. A. Credit Corp.*, 218 Va. 849 (1978).

⁷³ A trustee can only do with the trust property what the deed, either in express terms or by necessary implication authorizes him to do. *William v. Jones*, 165 Va. 398, 182 S.E. 280 (1935).

⁷⁴ *Guthrie v. First Huntington Nat' Bank*, 184 S.E.2d 628 (W. Va. 1971); see generally *Schmucker v. Walker*, 226 Va. 582, 585, 3113 S.E.2d 108, 109-10 (1984).

⁷⁵ See generally *Giannotti v. Hamway*, 234 Va. 14, 387 S.E.2d 725, 731 (Va. 1990).

⁷⁶ VA. CONST. OF 1971, art. IV, §14 provides, in part:

The General Assembly shall not grant a charter of incorporation to any church or religious denomination, but may secure the title to church property to an extent to be limited by law. See also VA. CONST. OF 1971, art. I, §16 (Religious Freedom Act).

⁷⁷ VA. Code Ann. §57-8 (Michie 1995) provides, in part:

The circuit court of the county or the circuit or corporation court of the city, or the judge thereof in vacation, wherein there is any parcel of such land or the greater part thereof may, on the application of the proper authorities of such church diocese, religious congregation, church or religious society or branch or division thereof, from time to time appoint trustees, either where there were, or are, none or in place of former trustees, and on such applications and without notice to the trustees change those so appointed whenever it

may seem to the court or judge proper to effect and promote the purpose and object of the conveyance, devise, or dedication, and the legal title to such land shall for that purpose and object be vested in the trustee for the time being and their successors.

⁷⁸ VA. Code Ann. §57-16 (Michie 1995) provides, in part:

(1) **How property acquired, held, transferred, etc.** – Whenever the laws, rules or ecclesiastic polity of any church or religious sect, society, or denomination commits to its duly elected or appointed bishop, minister, or other ecclesiastical officer, authority to administer its affairs, such duly elected or appointed bishop, minister, or other ecclesiastical officer shall have power to acquire by deed, devise, gift, purchase, or otherwise, any real or personal property, for any purpose authorized and permitted by its laws, rules, or ecclesiastic polity, and not prohibited by the laws of Virginia, and the power to hold improve, mortgage, sell, and convey the same in accordance with such laws, rules, and ecclesiastic polity, and in accordance with the laws of Virginia.

⁷⁹ VA. Code Ann. §57-12 (Michie 1995).

⁸⁰ VA. Code Ann. §57-15 (Michie Supp. 1999).

⁸¹ *Id.*

⁸² VA. Code Ann. §57-15.1 (Michie 1995) provides, in part:

Any order entered pursuant to §§57-14 and 57-15 may provide that any instrument evidencing a debt secured by a deed of trust or mortgage made in behalf of a church diocese, congregation, church or religious denomination or society or branch or division thereof, hereinafter referred to inclusively as: church," may be signed without personal liability by the treasurer or other fiscal officer of such church and there upon become the obligation solely of the church named therein.

⁸³ *Norfolk Presbytery v. Bollinger*, 214 Va. 500, 505, 201 S.E.2d 752, 756-57 (1974). **V**

