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W. Garrett Flickinger

Sheryl Scheible

Christian G. Fritz

LEGISLATURE TAMPERS WITH RECORDING ACT

W. GARRETT FLICKINGER,* SHERYL SCHEIBLE,** and CHRISTIAN G. FRITZ***

During the recent session of the New Mexico Legislature a bill has quietly passed both houses and been signed by the governor without that careful consideration of its effect the public has a right to expect. H.B. 231,[1] introduced by Representative Thomas Foy, drastically changes New Mexico's Recording Act. Our Act has been easily identified as a "notice" type act, an act concerned with protecting the *bona fide* purchaser, mortgagee, or judgment creditor as opposed to the "race" type act which seeks only to establish an absolute record that extinguishes the rights of those who are slow to reach the county clerk's office.[2] The amendment creates a form of mini-"race" inside our "notice" statute by eliminating the traditional concept that possession of land by someone other than the seller, mortgagor, or judgment debtor puts one on inquiry notice of any claims the possessor may have. We say mini-"race" because this change only applies when the possessor's claim is based on a real estate contract. Deeds, mortgages, leases, and other interests in property are not affected. In other words, this new act will cause the greatest harm to those who purchase by real estate contract, normally those people who face the greatest financial struggle to acquire realty.

Why this drastic change? It appears to be an effort by the legislature to reverse a judicial decision.[3] Such legislative responses are not in themselves wrongful; in fact they often lead to legal reform. In this case,

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* Professor of Law, University of New Mexico School of Law. B.A., Yale University; J.D., University of Michigan.

** Associate Professor of Law, University of New Mexico School of Law. A.S., J.D., University of North Carolina; LL.M., Yale University.

*** Assistant Professor of Law, University of New Mexico School of Law. B.A., Ph.D., University of California, Berkeley; J.D., University of California, Hastings College of Law.

1. Act approved March 2, 1990, ch. 72, 1990 N.M. Laws ____ (to be codified at N.M. STAT. ANN. § 14-9-3). The bill changed the Recording Act as shown in the italicized portions.

> BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF NEW MEXICO:
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> Section 1. Section 14-9-3 NMSA 1978 (being Laws 1886-1887, Chapter 10, Section 3, as amended) is amended to read:
>
> "14-9-3. *UNRECORDED INSTRUMENTS—EFFECT.*—No deed, mortgage or other instrument in writing not recorded in accordance with Section *14-9-1 NMSA 1978* shall affect the title or rights to, in any real estate, of any purchaser, mortgagee in good faith or judgment lien creditor, without knowledge of the existence of such unrecorded instruments. *Possession alone based on an unrecorded executory real estate contract shall not be construed against any subsequent purchaser, mortgagee in good faith or judgment lien creditor either to impute knowledge of or to impose the duty to inquire about the possession or the provisions of the instruments.*"

2. In fact only two states, North Carolina and Louisiana, still have pure "race" recording statutes.

3. Citizens Bank of Clovis v. Hodges, 107 N.M. 329, 757 P.2d 799 (Ct. App.), *cert. denied*, 107 N.M. 74, 752 P.2d 789 (1988). For a discussion of *Citizens Bank of Clovis*, see Survey, *Property Law*, 20 N.M.L. REV. 373, 399-401 (1990) (this issue).

however, the potential harm to the general public far outweighs whatever specific remedial effect intended by the law. Indeed, failure to thoroughly study the consequences of the law has far reaching effects almost certainly unintended by the legislature.

Inserting this mini-"race" exception into our "notice" statute not only makes New Mexico a jurisdictional aberration, but undermines our current recording statute. No other notice jurisdiction apparently has such a provision. This is not surprising because such an exception is totally antithetical to the basic concept of the "notice" type statute.

The *bona fide* purchaser is one of the oldest and most venerable of legal concepts. A *bona fide* purchaser is one who has paid value without notice of any defect in the title of his seller.[4] Until this year our recording statute followed this concept by protecting the subsequent purchaser (mortgagee or judgment lien creditor) "without knowledge of the existence of such unrecorded instruments."[5] Possession by someone other than the seller has always been regarded as placing the subsequent purchaser on notice to inquire as to the interests, if any, of the possessor. A failure to make such inquiry results in a judicial inference that the subsequent purchaser had notice of any potential claims of the possessor.[6] Under such circumstances, the subsequent purchaser no longer has *bona fide* status. Thus, it makes little sense in the real estate business to disregard the fact that the possessor is not the seller, especially when the possessor is purchasing the land under a real estate contract.

Beyond being an unwise change that disrupts our basic statutory scheme, the fact is that this new provision is unlikely to accomplish the purpose for which it was introduced, namely to insulate a judgment creditor from the possessing rights of a vendee. In the first place, this change does not alter the previous judicial decisions interpreting real estate contracts. The New Mexico courts have ruled that once a valid contract has been signed, the doctrine of equitable conversion converts the seller's interest into personalty[7] or at best, if realty, a future interest.[8] Thus no judgment creditor will be able to take advantage of the new provision because the interest is no longer realty for purposes of Section 39-1-6.[9] However, the subsequent purchaser or mortgagee would be able to take the property from the vendee even if he or she knew that someone other than the seller was in possession, regardless of the amount of the purchase price already paid to the seller. While it is true that the effect of the Recording Act is to grant such right of priority, the purpose of the New Mexico act was to grant this power only to purchasers and mortgagees "without notice." If the notice requirement is to be eliminated, it should be done with careful thought and apply to all instruments.

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4. *E.g.*, Jeffers v. Martinez, 93 N.M. 508, 601 P.2d 1204 (1979).

5. N.M. STAT. ANN. § 14-9-3 (Repl. Pamp. 1988); *see supra* note 1.

6. *Citizens Bank of Clovis*, 107 N.M. at 331-32, 757 P.2d at 801-02 (citations omitted).

7. *See, e.g.*, *Citizens Bank of Clovis*, 107 N.M. at 333, 757 P.2d at 803 (citing Marks v. City of Tucumcari, 93 N.M. 4, 595 P.2d 1199 (1979)).

8. *See* First Nat'l Bank of Belen v. Luce, 87 N.M. 94, 529 P.2d 760 (1974).

9. N.M. STAT. ANN. § 39-1-6 (Cum. Supp. 1989).

In addition to failing to accomplish its ostensible purpose, the statute invites litigation under both common law principles and the United States Constitution. For example, given the New Mexico Supreme Court's adoption of the "prima facie" tort theory,[10] anyone taking advantage of this new provision in the Act may be liable to the vendee under that tort. In addition to the "prima facie" theory of liability, escrow agents as well as real estate agents may have a duty to insure that real estate contracts are recorded. Since the new change puts purchasers under these contracts at a substantial risk of harm,[11] and the effort required of their escrow and real estate agents is so minimal, a court may well impose such a duty.

Finally, individuals who have entered into real estate contracts before the effective date of the new provision may well challenge that law on a number of constitutional grounds. First, the fact that this provision singles out real estate sales contracts might give rise to an argument of impairment of contract. Second, the failure to include possessors under all other unrecorded instruments might well be regarded as a denial of "equal protection." There appears to be no rational reason for choosing only one of the many types of possessors under unrecorded documents for this change in the rules. Last, any attempt to use the new provision might violate "due process" since the change hardly guarantees "fair play and equal justice."

In sum, the New Mexico Legislature should reconsider its recent change of the state's Recording Act. That change seems destined to reap a harvest of lawsuits due to its intended and unintended consequences.

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10. Schmitz v. Smentowski, ___ N.M. ___, 785 P.2d 726 (1990).

11. In *Citizens Bank of Clovis*, the buyers had not only completed full payment of the purchase price under the contract, but had added $25,000 worth of improvements when the seller's judgment creditor attempted to foreclose. 107 N.M. at 331, 757 P.2d at 801.