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Decisions Committee
Section of Real Property
Probate & Trust Law
American Bar Association

Quarterly Report on Current Developments in Real Estate Law

April 1, 2005 to June 30, 2005

Prepared by:

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Committee on Decision

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This publication is intended to provide experienced real estate practitioners with information on recent decisions and writings affecting real estate practice. Although there are occasional reports of administrative or legislative decisions or related matters, the primary focus of the Report is on appellate court decisions. Members of the Committee are assigned to review all reported decisions in standard reporting services received in their libraries prior to the close of the stated reporting period. They forward their summaries those cases that they deem to be of interest to a nationwide audience. They forward their summaries and copies of the cases to the editor, who substantially edits the summaries and frequently adds comments.

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ALTERNATIVE DISPUTE RESOLUTION; ARBITRATION; CONTRACT PROVISION: Real estate broker that did not sign real property purchase agreement containing arbitration provision was entitled, as both signatories' agent, to enforce arbitration agreement against party to agreement. ***Westra v Marcus & Millichap Real Estate Inv. Brokerage Co, 28 Cal. Rptr. 3d 752 (Cal. App. 2005)*** discussed under the heading: "Brokers; Arbitration."

BANKRUPTCY; AUTOMATIC STAY; RELIEF FROM STAY; STATUS OF CREDITOR: In Missouri Chapter 7 bankruptcy, the debtor cannot defend a petition for relief from the automatic stay by a foreclosing mortgagee by arguing that the mortgagee has not produced the note and is not the original mortgagee. ***In re Martens, 2005 Westlaw 2417653, (8th Cir. BAP 10/3/05)***

The debtor, acting *in pro per*, perhaps had gotten wind, through the internet, of the problems that MERS is having with foreclosures in Florida. In the DIRT DD report of 9/16/05, it was noted that a Florida state court judge had dismissed a number of foreclosures where the record did not disclose that the party seeking foreclosure was in fact the mortgagee.

The debtor in the instant case claimed that the creditor here, a well known secondary market purchaser, was not the original lender who had loaned money to her secured by a mortgage on her home. She further alleged that the creditor had not produced the note. She claimed that seeking to foreclose without producing the note is a violation of the Fair Debt Collection Practices Act and also a violation of Missouri law.

The bankruptcy court held, and the BAP here affirmed, that these defenses were not relevant to an action for relief from the automatic stay. It noted that the debtor, in its original filing (Debtor at time of filing was represented by counsel), had listed Countrywide as a creditor, had acknowledge that the debt was in default and that there was no equity in her property. Hence, the debtor's own acknowledgments made a case for granting relief from the stay under the Bankruptcy Code standards.

The court went on to note, as *dicta*, that there is nothing in the FDCPA or Missouri law that requires production of the original note, so long as the mortgagee can show that indeed it is the lawful holder of the right to foreclose the mortgage Here, of course, the mortgagee had acknowledged that Countrywide was a mortgage creditor.

Comment: Holdings of this sort will move along a lot of bankruptcies that might get held up by this new focus on production of the note as the key to the foreclosure process. Although, indeed, many lenders do get possession of the note (and MERS did obtain the note in the DD referred to above), it is a fact that many secondary market purchasers move very quickly to move portfolios around very quickly and often do not complete the follow up to obtain the note. The note may be with the originator, may be with MERS, or may not be anywhere that any knows for sure.

This holding at least gets the lender past the bankruptcy. It is also fair warning that the *pro se* filers are onto the "note thing" and that secondary market mortgage investors are going to have to contend with that issue in a variety of manifestations over the next few months.

BANKRUPTCY; LANDLORD/TENANT; DAMAGES CAP; LETTERS OF CREDIT: Ninth Circuit affirms rule of *Mayan*, a landlord's application of letter of credit as security deposit is taken into account in computing bankruptcy cap on landlord's damages under 502(b)(6). ***AMB Prop., L.P. v Official Creditors for the Estate of AB Liquidating Corp.(In re AB Liquidating Corp.) 416 F3d 961(9th Cir 2005)***

In *In re Mayan Networks Corp. (Redback Networks, Inc. v. Mayan Networks Corp.,*206 B.R. 299 (9th Cir. BAP 2004) (the DIRT DD for 2/26/04) a Bankruptcy Appeals panel in the Ninth Circuit pronounced what has become accepted as "established wisdom" concerning the relationship between security deposits in the form of letters of credit and the bankruptcy cap on landlord's damage claims articulated in Bankruptcy Code section 502(b)(6). *Mayan* put the skids to the rosy suggestions of many landlord's lawyers that the "independence principle" – the notion that letters of credit stand by themselves as independent obligations of the issuing bank – would insulate letter of credit security deposits from the limits of the cap. Although, indeed, the bank is obligated to pay on the letter promptly, the court noted, this is as far as the "independence principle" takes us. If the bank has a right of recourse against the tenant or the tenant's assets, then in essence the obligation remains an obligation of the tenant and the tenant deserves the protection of the "cap."

The court went on to assert that if, in fact, the issuing lender has no recourse against the tenant or the tenant's assets, and the bank has issued the letter pursuant to the guaranty or security provided by some third party, then the letter of credit proceeds would not reduce the amount of damages that the landlord could pursue directly from the tenant. The limit is not on the amount of damages that the landlord can recover, the court said, but rather than the amount to which the tenant can be exposed. Of course, this statement was *dicta* in *Mayan*, where there was specific tenant security pledged for the letter of credit.

Many lawyers have been convinced by the logic of the *Mayan* decision and have concluded that is probably the way that the issue should come out, so *Mayan* has influenced thinking well beyond the Ninth Circuit. But it was still only a BAP decision. Now we have a Ninth Circuit Court of Appeals decision that upholds *Mayan* against a specific attack against it and the earlier authority that supports it.

In the instant case, the landlord had a $5 million damages claim. The bankruptcy cap limited the landlord's allowed claim to $2 million. Further, the $1 million security deposit the landlord held was not applied just against landlord's gross $5 million claim (reducing it to $4 million), but was applied against the $2 million capped claim.

Thus, landlord's remaining allowed claim was only $1 million. Landlord could keep the security deposit, but the allowed remaining claim was only $1 million beyond that.

Reporter's Comment 1: Landlords have had enough experience with defaulting tenants to know they need front-end protection, which they obtain by requiring security deposits at the start. During the dot.com boom, it was common to see landlords taking letters of credit-covering from 6 to 18 months of rent-posted by tenants' lenders or investors. (Letters of credit were popular with tenants because they didn't require real money, and were attractive to landlords because it was thought that the independence principle made them supposedly more invulnerable to attachment than plain cash,

This case demonstrates that the existence of a security deposit does not necessarily provide as much protection as the landlord would like when her tenant goes under. If tenant files bankruptcy, landlord's recovery is capped by 11 USC §502(b)(6) at one year's rent (in most cases).

Judge Klein's concurrence in *Mayan* suggests that a security deposit consisting of a letter of credit not collateralized by the debtor's property might be treated differently, but how many issuers of such letters would be willing to do so without full collateral?)

Reporter's Comment 2: Under this formula, risk-averse landlords would be advised to seek security deposits equal to a full year's rent, not just six months, if they can get them. (An even larger security deposit might look nicer, but it would not do much better, because the excess over the capped claim-the one year's rent-would probably just have to be turned over to the bankruptcy trustee.)

Editor's Comment 1: The editor is not so sure about the proposition in the Reporter's comment 2, above. In *Mayan,* Judge Klein wrote an important concurrence that suggested a more dramatic result when the letter of credit security deposit exceeds the capped rent. His opinion appeared to stat that if the letter of credit exceeds the amount of the tenant's "capped" damages (not the facts in *Mayan),* but does not exceed the landlord's total damages claim, the landlord ought to be able to seek application of the letter of credit anyway, and that the party that should suffer the loss of the restriction of rights against the bankrupt tenant ought to be the lender. In other words, if the damage claim is $5 million, as here, and the bank has issued a $5 million letter of credit as security, but, as here, the "capped" damages claim if $2 million, the landlord could make a claim on the whole $5 million, but the bank would be limited to a right of recourse against the tenant of $2 million.

The landlord in the instant case attempted to invoke Judge Klein's *Mayan* concurrence as supporting a different outcome here. The court did not agree, indicating that Judge Klein's opinion was fully consistent with the outcome in the instant case – where the letter of credit security deposit was equal to or less than the "capped" claim and where the issuing bank had recourse against the debtor tenant or its property as security. Further, although not called upon to "buy in" to all the views expressed by Judge Klein, there was no indication that it disagreed with Judge Klein's views.

Of course, knowing of this risk, banks will certainly protect themselves from this happening. But the fact of the risk will certainly alter the dynamics of the bargaining for letters of credit as security deposits.

The Reporter in this case was Professor Roger Bernhardt of the Golden Gate Law School in San Francisco, writing in the California Real Property Report. The editor has extensively revised the report, and truncated the comments as well. So Roger bears no responsibility for any inaccuracies or ambiguity above.

BANKRUPTCY; LANDLORD/TENANT; RENT; DAMAGES CAP; LETTERS OF CREDIT: Fifth Circuit reverses holdings of bankruptcy court and district court, and holds that landlord's retention of letter-of-credit proceeds in excess of bankruptcy cap on landlord's damages under 502(b)(6) is permissible because Sec. 506(b)(6) cap was not triggered where landlord did not file claim in tenant-debtor's bankruptcy case.

EOP-Collonade of Dallas Ltd. P'ship v. Faulkner (In re Stonebridge Techs., Inc.), 2005 U.S. App. LEXIS 24024 (5th Cir. Tex., 11/08/05)

This case involved a claim by the bankruptcy trustee (on behalf of the tenant-debtor in a Chapter 11 proceeding) that the Bankruptcy Code sec. 506(b)(6) cap limited the lessor's draw on a letter of credit provided as a security deposit for the tenant's obligations under the lease (Under sec. 502(b)(6), a landlord's claim for early termination of a lease is limited to the rent due under the lease for the greater of one year or 15 percent, not to exceed three years.) Because the letter of credit draw exceeded the capped amount, the trustee sought reimbursement to the estate of the excess.

The security deposit consisted of both cash, in the amount of $105, 298, and a letter of credit, in the amount of $1,430,065. The letter of credit was secured by a certificate of deposit from the tenant in the amount of $1,250,000, to reimburse the bank if there was a draw under the letter of credit. After the tenant filed its bankruptcy petition, the tenant-debtor and the landlord agreed that the lease would be rejected, the effective date of rejection to occur between October 1 and October 23, 2001. Prior to the court date scheduled for the court to issue its order approving the rejection (October 23, 2001), the landlord initiated a draw request against the issuing bank, and the bank in fact paid the full amount of the letter of credit to the landlord on October 30, 2001. On November 8, 2001, the bankruptcy court entered a *nunc pro tunc* order approving the lease rejection and making the lease rejection retroactively effective as of October 1, 2001. But, according the Fifth Circuit, "The record conclusively demonstrates . . . that [the landlord] never filed a proof of claim for its actual lease rejection damages following the bankruptcy court order rejecting the lease and approving [the landlord's] administrative rent claim."

The bank subsequently sought relief from the automatic stay to apply the certificate of deposit it held as security for the tenant-debtor's reimbursement obligations under the letter of credit. The bankruptcy trustee and the bank reached a compromise settlement agreement whereby the trustee would allow the bank to apply the certificate of deposit in exchange for an assignment of the bank's claims against the landlord for its alleged improper draw under the letter of credit. The trustee then brought an adversary action against the landlord, claiming that the landlord had breached the lease by prematurely drawing under the letter of credit and retaining an amount in excess of the sec. 502(b)(6) cap.

The bankruptcy court ruled that because the letter of credit was part of the security deposit, it was subject to the sec. 502(b)(6) cap, and also held that the landlord had breached the lease by drawing on the letter of credit before the bankruptcy court's *nunc pro tunc* order had been entered. The bankruptcy court awarded damages to the bankruptcy estate (for "negligent misrepresentation" by the landlord regarding its right to draw on the letter of credit) in the amount of $180,000 based on the difference between the amount the landlord drew under the letter of credit and the amount the issuing bank received from the certificate of deposit, and damages in the amount of $2,267 for breach of the lease, based on the difference between what the landlord would have been entitled to receive under sec. 502(b)(6) (less the cash security deposit) and the amount the issuing bank collected on he certificate of deposit. The district court subsequently affirmed the bankruptcy court's ruling, on January 30, 2004.

The Fifth Circuit reversed the rulings of the bankruptcy court and district court. According to the Fifth Circuit, the sec. 502(b)(6) cap "prevents a lessor who files a claim against the estate from reaping an unfair share of the bankruptcy estate over the remaining pool of unsecured creditors." The court also reiterated that it is well-settled in the Fifth Circuit that "letters of credit and the proceeds therefrom are not property of the debtor's bankruptcy estate."

The court then reasoned that by its terms, sec. 502(b)(6) applies only to claims against the bankruptcy estate, and that claims under that section must be formally filed with the bankruptcy court and are not "assumed" simply because the tenant-debtor assumes or rejects a lease under sec. 365. According to the Fifth Circuit (after citing applicable case law), "Stated simply, the claim of a lessor against the assets of the estate is an essential precondition to applying the damages cap at all." Based on this reasoning, the Fifth Circuit held that no inquiry into the appropriate interpretation of sec. 502(b)(6) was necessary in this case because the landlord did not file a claim against the estate. (The court also stated, in a footnote, that "We also note that sec. 502(b)(6) does not apply to limit administrative expense claims made by the landlord based upon the continued use of the premises after the filing of the bankruptcy petition.") The court rejected the trustee's argument that the letter of credit was subject to the sec. 502(b)(6) cap because it was part of the security deposit under the lease, pointing out that (unlike preference law) the trustee is not permitted under the Bankruptcy Code to separately sue a lessor for receiving property of the estate (by bringing an avoidance action) simply because it exceeds the sec. 502(b)(6) lease cap.

The Fifth Circuit distinguished two recent security-deposit/letter-of-credit cases, *In re PPI Enterprises, Inc*., 324 F.3d 197 (3rd Cir. 2003) and *In re Mayan Networks Corp*., 306 B.R. 295 (B.A.P. 9th Cir. 2004), by noting that (unlike the present case) in each of these cases the landlord had actually filed a claim against the bankruptcy estate seeking to recover lease-rejection damages in excess of the amount of the security deposit.

The Fifth Circuit also found that the landlord had not prematurely drawn against the letter of credit because such a draw was permitted under the "Monetary Default" and acceleration provisions of the lease, and the landlord's motion for payment of rent filed in the bankruptcy proceeding constituted sufficient written notice to the tenant-debtor of non-payment of the rent owing under the lease. The court noted that "the measure used to calculate accelerated damages under the Lease is the same measure that would be used to calculate the damage to a lessor from the rejection of a lease when not applying the sec. 502(b)(6) cap." The court also ruled that lease rejection may be retroactively applied, and therefore the fact that the actual court order setting the retroactive lease-rejection date was not entered until after the landlord's draw on the letter of credit was irrelevant (especially because the tenant-debtor had approved the earlier effective rejection date).

Comment 1: Apparently the reason why, in this case, the landlord did not file a claim against the bankruptcy estate for lease-rejection damages was that the tenant-debtor's obligations were substantially (though not totally) secured by the letter of credit, which the landlord drew upon when the tenant-debtor defaulted under the lease. According to the Fifth Circuit (in a footnote), "It is undisputed that [the landlord] would have been limited to rejection damages from [the tenant-debtor's] estate of $1,353,032.02 if it had filed a claim against the estate." This is certainly good news for landlords where the amount of the letter of credit is sufficient to fully secure the landlord's damages under the lease. Even if the amount of the letter of credit is not fully sufficient to cover the landlord's damages, it will often make sense (at least in the Fifth Circuit) to draw on the letter of credit and forego filing a claim in the tenant-debtor's bankruptcy proceeding and risk being subjected to the sec. 502(b)(6) cap.

Comment 2: In its opinion, the Fifth Circuit cites and quotes from, in its opinion, an impressive body of case law and commentary in support of its position that sec. 502(b)(6) applies only where the landlord has actually filed a claim against the estate in the bankruptcy court. It will be interesting to see if other courts follow the holding in this case.

Comment 3: Interestingly, the bankruptcy court found that the landlord's breach-of-lease damages were only $2,267 (the excess of the certificate of deposit securing the tenant-debtor's reimbursement obligation to the issuing bank over the landlord's capped claim of $1,353,032, less the cash security deposit of $105,299). The difference of $180,066 between the face amount of the letter of credit and the certificate-of-deposit collateral was awarded to the trustee only as the assignee of the issuing bank (in the form of damages for the allegedly unwarranted and premature presentation of the letter of credit.) But there is no indication that the letter of credit was expiring, and the issuing bank still would have been obligated to pay the full amount to the landlord if it had presented its draft after the later entry of the bankruptcy-court order retroactively rejecting the lease.

Comment 4: The facts in the *Stonebridge* case required the court to confront the other side of the issue addressed by the Third Circuit in *PPI Enterprises*; namely, whether a landlord can retain letter-of-credit proceeds in excess of the cap. With respect to the *PPI* and *Stonebridge* cases, an excellent article on the issues raised in these cases, "Courts Limit Benefits to Landlords under Letters of Credit," by Daniel J. Carragher, appeared in the July 2003 issue of the American Bankruptcy Journal (2003 ABI JNL. LEXIS 126). Note in particular the following excerpts from this article (which was published prior to the Fifth Circuit's overruling of the bankruptcy court and district court opinions in the *Stonebridge* case):

> "The Stonebridge decision acknowledges the importance of the independence principle, but much more clearly attempts to preclude the use of a letter of credit to avoid the statutory cap of § 502(b)(6). As in PPI Enterprises, the court placed great emphasis on the lease provisions allowing the posting of a letter of credit as part of the security deposit. Simply characterizing a letter of credit as security, however, does not resolve the § 502(b)(6) dilemma. Where a debtor has posted the security directly, § 506(a) and (d) will limit the landlord's rights in the security to recovery of the allowed claim. Where the "security" has been provided by a third party, the issue should be purely one of contract interpretation, and one-year or 15-percent limitations of § 502(b)(6) and the provisions for claims secured by a debtor's property in § 506 should not apply. The Code is silent on the issue, and the references to security deposits posted by a debtor in the legislative history do not require the disgorgement of third-party letter-of-credit proceeds in excess of the cap. When a landlord has bargained for the third-party credit enhancement as a condition to entering into the lease, there is nothing in the [Bankruptcy] Code or legislative history that requires that a letter of credit be treated differently than a guaranty from a solvent third party.
>
> The disgorgement issue in the *Stonebridge and Musika* cases will continue to be the subject of debate in the courts. Until the higher courts resolve the issue, landlords cannot rely on letters of credit to provide the full extent of the bargained protection in the tenant's bankruptcy. In the meantime, attention should be paid to negotiating the letter-of-credit and lease default provisions to permit the landlord to draw on the funds at the earliest possible date after the tenant's bankruptcy."

The *Stonebridge* and *PPI Enterprises* cases provide reassurance that landlords will be free to draw on letters of credit without interference from the bankruptcy court. The requirements of the perfect tender rule still may require relief from the automatic stay to permit a landlord to give notices of default or acceleration required by the terms of the letter of credit as conditions to drawing. A carefully drawn letter of credit that permits presentment upon the tenant's bankruptcy or failure of payment should ordinarily dispense with such requirements.

Comment 5: The Fifth Circuit, in the *Stonebridge* case, strongly reaffirms (as does the vast majority of bankruptcy cases) the "independence principle" with respect to letters of credit. The independence principle provides that a letter of credit is an independent third-party obligation and the proceeds thereof are not the debtor's property even if the letter of credit is secured by the debtor's property. *See, e.g., In re Wedtech Corp.*, 187 B.R. 105, 107 (Bankr. S.D.N.Y. 1995) ("When a debt is secured by collateral pledged by a third party, the security interest does not give rise to a secured claim against the debtor's estate"). See also Christopher Leon, Letters of Credit: A Primer, 45 Md. L.Rev. 432, 442-43 (1986); Kimberly S. Winick, Tenant Letters of Credit, Bankruptcy Issues for Landlords and Their Lenders, 9 AM. BANKR. INST. L. REV. 733, 740 (2001) ("Of course, if the landlord can rely on the tenant's nonperformance of other obligations under the lease, it should do so. Even though the tenant is not a party to the letter of credit, the tenant may try to argue that terms of the letter of credit that permit a draw merely because the tenant is in bankruptcy are unenforceable *ipso facto* clauses. Such other obligations include, but obviously are not limited to, timely payment of rent, timely payment of common area charges, repair and maintenance of the property in conformance with agreed standards, payment of taxes, and maintenance of adequate insurance with the landlord (and its mortgage lender) named as additional insureds. Additionally, the landlord should be able to draw under the letter of credit without the tenant's cooperation. For example, the draw should not be conditioned on the presentation of documents that must be executed by the tenant, as the landlord cannot compel execution by a tenant in bankruptcy. Similarly, draws should not be conditioned on the landlord's prior notice of default, notice of acceleration, or demand on the tenant for payment; upon commencement of the tenant's bankruptcy case, default notices, notices of acceleration, and demands for payment for amounts due pre-bankruptcy are stayed by section 362(a)").

The supposed erosion of the "independence principle" by the recent *In re Mayan Networks Corp*. case (9th Circuit) and *AB Liquidating* case applies only with respect to the specific fact situation where a landlord holds a letter of credit as the security deposit under a lease and the issuer's right to reimbursement under the letter of credit is fully secured by the tenant-debtor's collateral. (In the *In re AB Liquidating Corp.* case, 416 F3d 961(9th Cir 2005), the Ninth Circuit affirmed the rule of the *In re Mayan Networks Corp*. case; *i.e.,* that a landlord's application of a letter of credit as a security deposit is taken into account in computing the bankruptcy cap on the landlord's damages under sec. 502(b)(6).)

Comment 6: To protect themselves, some landlords may require that the letter-of-credit issuer not secure the reimbursement obligation with the tenant's assets. Other suggested strategies to avoid issues involved with regard to application of the § 502(b)(6) cap include the following: separate the security deposit for the rent and other lease-performance obligations of the tenant from any tenant-improvement repayment obligations and secure that obligation with a separate secured loan and promissory note from the tenant (to avoid having it characterized as a lease-rejection claim); have a guarantor separately provide the security (although this could be problematic if the guarantor becomes a debtor in bankruptcy); and provide that the letter of credit is in "lieu of" a lease security deposit). Whether any of these suggested strategies will actually be effective, and accepted as valid by bankruptcy courts, remains to be seen. See Jo-Ann Marzullo, "Letters of Credit: No Panacea for Tenant Defaults," Retail Law Strategist, Oct. 2004, p.1; Michael P. Richman, "Protect Your Right to Tap Bankrupt Tenant's Letter of Credit," Commercial Lease Law Insider, June 2004, p. 5.

Note also Judge Klein's suggestion, in his concurring opinion in the *In re Mayan Networks* case, that letter-of-credit issuers protect themselves "from bankruptcy risk by requiring creditworthy co-obligors or insisting that security deposits come from sources, and with refund obligations, that are not property of the estate." But it may be advisable to have any third-party guaranty of reimbursement for payment under the letter of credit contain a specific waiver by the guarantor of any reimbursement, contribution, subrogation or indemnity rights against the tenant-debtor. Otherwise the bankruptcy trustee, or other creditors, could argue that payment by the guarantor is an "indirect payment" from the tenant-debtor, and it will be uncertain who gets the first right to the statutory cap — the guarantor or the letter-of-credit issuer. Without such a waiver, the guarantor and the letter of credit issuer likely would lock horns as to who is first entitled to the capped amount of the rental claim.

Editor's Comment 1: The editor has set forth exactly Jack's reportage of the case. Based upon this description, it appears that there was a settlement between the trustee and the issuing bank, presumably approved by the bankruptcy court, that permitted the bank to collect fully its security interest in the certificate of deposit that secured the letter of credit security deposit. Thus, the question never arose whether the bank had a legal right to collect from the tenant in reimbursement for the payment on the letter of credit in an amount in excess of the 502(b)(6) cap. That strikes the editor as the central question in all of this, and before landlord's lawyers start dancing all over the internet law journals, we need to recognize that in this case the application of the letter of credit to satisfaction of the landlord's claim did not place the tenant's estate in jeopardy in an amount in excess of the capped claim. That question, it strikes the editor, is the central question.

It is one thing to say that the landlord can collect on the letter of credit if it does not make a claim for damages in the tenant's bankruptcy. It is quite another to conclude that the issuing bank may seek reimbursement from the tenant's estate in excess of the capped amount when it pays out on that letter of credit. We don't yet have an affirmative answer to this question. Banks will certainly now begin to draft letter of credit security agreements that will protect them from being liable on the letter of credit in excess of amounts that they can collect from the estate. So the landlords' victory here may be short lived.

Editor's Comment 2: Note that the court also permitted forfeiture of the relatively small cash security deposit, apparently on the theory that such amount did not exceed the cap.

The reporter for this item was Jack Murray of First American Title Insurance, Chicago office.

BANKRUPTCY; LIENS; JUDGMENT LIENS; AVOIDANCE: Plain meaning of 11 USC §522(f)(2) – Trustee's avoidance power – requires avoidance of creditor's judicial lien, even though that lien is senior to consensual lien. ***Moldo v Charnock (In re Charnock)318 BR 720 (BAP 9th Cir Dec. 15, 2004)***

Moldo was appointed state court receiver in the dissolution proceedings of debtor Paula Charnock. In 1996, Moldo recorded an abstract of judgment, covering $56,072 in fees and costs incurred in the administration of the receivership estate. Charnock owned a residence that she refinanced in 2002, paying Moldo $28,000 from the proceeds of the loan. A deed of trust was recorded at that time evidencing the lender's lien. A year later, Charnock filed for Chapter 7 bankruptcy protection and moved to avoid Moldo's judicial lien under 11 USC §522(f)(2). The sum of the balance of the refinancing loan plus the amount of Charnock's homestead exemption exceeded the stipulated value of the property. The bankruptcy court granted Charnock's motion to avoid the lien.

The appellate panel affirmed. As the court noted, Congress chose among conflicting policies and ultimately favored consensual lienholders over judicial lienholders. The clear legislative intent of the changes to the bankruptcy statute was to override case law holding that a judicial lien could not be avoided if it was senior to a nonavoidable mortgage lien, and the total of all mortgages against the property exceeded the value of the property. Congress deliberately determined that judgment lien creditors would be treated differently from consensual lien creditors. The Bankruptcy Code provision is intended to preempt state law lien priorities that would apply outside bankruptcy; the policy favoring preservation of the homestead exemption does not create a windfall for, or confer a benefit not intended by Congress on, the debtor in a consumer bankruptcy proceeding.

Reporter's Comment: This case involved a judgment lien of about $70,000, a deed of trust of $370,000, and a debtor's homestead protection of $75,000, against a property valued at only $435,000. The lien, the deed of trust, and the homestead totaled $515,000, or $90,000 more than the worth of the property; at least one of those interests had to suffer.

There is no easy resolution of this issue. The judgment lien is superior to the deed of trust but inferior to the homestead, while the deed of trust is inferior to the judgment lien but superior to the homestead, and the homestead is superior to the judgment lien but inferior to the deed of trust. Everybody is superior to one party and subordinate to another party. It is classic lien circuitry!

While this is a hard issue for state courts to resolve (see *Bratcher v Buckner* 90 CA4th 1177, 109 CR2d 534 (2001), cited in *Charnock*), it is apparently a slam dunk for bankruptcy courts, since the plain meaning of §522 of the Bankruptcy Code is that the judicial lien may be avoided as impairing the homestead exemption even though the impairment happens only because of the deed of trust, which came after the judicial lien. Put another way: If the debtor had filed bankruptcy before putting a deed of trust on her property, the judicial lien would have been allowed, since at that stage it did not impair her statutory homestead exemption. But if the debtor later encumbers her liened property with a deed of trust, leaving her with less than $75,000 of equity in the property, then to the extent her homestead has been impaired, the prior judicial lien can be avoided.

Reporter's Comment 2: So, the judicial lien creditor in this situation is the real loser. But who is the winner? The BAP was a little less willing to call that result (it was not before the panel on this appeal), but the judges made their sentiments clear: The winner should be the bankrupt debtor rather than the beneficiary of the deed of trust. The deed of trust is to stay as far below the judgment lien as it always was; the amount avoided enhances the homestead protection instead.

Thus, assuming the property was encumbered by a judgment lien of $70,000 and worth $435,000 when the deed of trust was put on, there was only $365,000 of remaining value to secure the $370,000 deed of trust; it was undersecured by $5000. Avoiding the $70,000 judgment lien could add the missing $5000 to the beneficiary's security, or it could, as suggested here, add $70,000 to the debtor's homestead exemption and nothing to the deed of trust. That latter result is not surprising, because that's what bankruptcy is supposed to be about: protecting debtors even at the expense of their creditors.

It is too bad that the deed of trust beneficiary did not also appeal. Its loan was apparently a refinance, meaning that there was a good chance it could have claimed subrogation rights for the old loan it paid off, which loan probably was superior to the judgment lien. That would have generated a whole different set of calculations.

The Reporter for this item was Professor Roger Bernhardt, of Golden Gate Law School in San Francisco, writing in the CEB California Real Property Law Reporter.

BROKERS; ARBITRATION: Real estate broker that did not sign real property purchase agreement containing arbitration provision was entitled, as both signatories' agent, to enforce arbitration agreement against party to agreement. ***Westra v Marcus & Millichap Real Estate Inv. Brokerage Co, 28 Cal. Rptr. 3d 752 (Cal. App. 2005)***

In 1999, the Westras purchased a gas station from Skyline. Both the Westras and Skyline were represented in the purchase transaction by Marcus & Millichap Real Estate Investment Brokerage (MM). The gas station was occupied by tenant Paul Tran, who at some point declared bankruptcy and disappeared. The Westras sued MM, alleging fraud and other claims related to Skyline's and MM's failure to disclose their purported knowledge of Tran's financial problems. Skyline and MM moved to compel arbitration of the claims, based on an arbitration provision in the purchase agreement that had been initialed by Skyline and the Westras, both of whom had also signed the agreement – but not by MM, which was not a signatory to the agreement. The trial court ordered that the Westras' claims against Skyline be arbitrated, but found that the arbitration provision did not apply to the Westras' claims against MM.

The court of appeal affirmed the arbitration order as to Skyline, but reversed the trial court's denial of arbitration as to MM, and remanded. Ordinarily, an arbitration provision in an agreement is only enforceable by the parties to that agreement. The court acknowledged that CCP §1298, as the Westras argued, requires that a real estate agent initial the arbitration provision of a contract between that agent and its client in order to create a binding arbitration agreement. However, the court held that the Federal Arbitration Act (9 USC §§1-16) preempts state arbitration laws and, thus, §1298 was inapplicable to this case. *See Hedges v Carrigan* 117 CA4th 578, 583, 11 CR3d 787 (2004).

The court agreed with MM that although it was not a signatory to the arbitration agreement, it was entitled, under the exception to the parties – only enforcement rule, to enforce the arbitration agreement as the agent for the parties to the arbitration agreement. The court rejected the Westras' claims that MM was not the signatories' agent, pointing to the Westras' pleadings that MM owed them the fiduciary duties of an agent, precluding the Westras' later protestations that MM was not its agent or that of Skyline.'

Reporter's Comment: The Marcus & Millichap brokerage was able to demand arbitration as agent of the litigants even though the deposit receipt recited that the brokerage had no fiduciary relationship to them. Thus, that clause did not hurt the broker-but I wonder whether it would help when it matters. Can an agent really make itself a nonfiduciary by including a clause in a contract of sale between vendor and purchaser, that was not intended to apply to it anyway, and which the principals might not have been able to eliminate even had they wanted to? For resolution of that much more interesting issue, we will just have to wait and see.

Editor's Comment: If the instrument that the parties executed was a broker-supplied instrument, as is often the case even in commercial deals in California (sigh), then wouldn't any broker using such an instrument, at least in the future, be obligated to note that even where the broker does not execute the arbitration agreement, the broker can benefit from it? If the broker fails to do so, isn't it liable for providing an instrument that is misleading and ambiguous when it knows or should know of the problem?

It would be ironic if the language of the instrument was so problematic that a duty imposed by federal law would not be obvious – but isn't that the situation here? If the brokers don't like the duty, then get out of the business of supplying forms so the parties can avoid attornies.

The Reporter for this case was Professor Roger Bernhardt of the Golden Gate University School of Law in San Francisco.

CONDOMINIUMS; USE RESTRICTIONS; SALE OF UNITS: Condominium association, through amendment of bylaws, can restrict sale of small studio apartments in complex of much larger apartments so that studios can be sold only to owners of one of the larger apartments. ***Demchick v. 90 East End Ave. Condominium, 796 NYS2d 72 (App. Div. 2005)***

The condominium project in question consisted of a number of thirty eight large luxury apartments and five small studios. The studios were located on the second floor, along with the gym, the children's playroom, and the laundry facilities. The sale agent for the developer told a number of prospective buyers that these smaller units were limited specifically for use for household staff or guests of owners of the larger apartments, and that they could not be sold separately.

Plaintiffs acquired one of the larger apartments and one of the studios, which they used for storage. They claimed that their agent did not tell them that resale of the studio was restricted, and indeed it turned out that the condominium documents did not restrict resale of the studios.

Subsequent to plaintiffs' purchase of their units, another owner proposed to sell one of the studios separately, and the association board discovered the fact that the condominium documents and the expectations of most of the owners did not coincide with respect to the saleability of the studio units. The board initiated a vote to amend the bylaws to restrict such sale, and the amendment passed by majority vote of the unit owners despite plaintiffs' objection.

The plaintiffs then brought suit to set aside the restriction as an unlawful restraint on alienation. The trial court found the restriction to be an unenforceable restraint on alienation, and granted plaintiffs' summary judgment. In a very brief opinion, and apparently as a matter of first impression, the appeals court reversed.

The court found that the restriction was consistent with a reasonable motive to maintain the nature of the entire building as a high end luxury residence and that, although unlimited in duration, the restriction could always be changed by a majority vote of the residents. It further noted that New York statutes permit condominium associations to restrict sale or leasing of units, subject to the common law doctrine against unreasonable restraints. In context, the court ruled, this was not an unreasonable restraint.

Comment 1: The editor views this case as a moderate and balanced review of a specific sale restraint, and not a license for every condominium association to restrict the sale of units indiscriminately. The smaller units clearly were, by design and function, of a nature distinct from the primary residential character of the building, and the bylaws amendment likely corrected an oversight by the developer (or perhaps the developer's lawyer had warned it about the restraints on alienation doctrine.)

If condominium interests in New York have authority generally to amend their bylaws to protect the "high end" character of their residences and thus maintain the value of their investment, then the editor is not particularly troubled or surprised by this ruling New York applies the "business judgment rule" to condominium decisions generally – philosophically the most permissive of standards for review of these decisions, although in practice there may not be a lot of difference among the various standards.

Comment 2: Some commentators have noted that the most common distinction observed between condominium and coop developments in New York is that the former are freely transferable while coop units can normally be sold only to persons approved by the coop board. This likely is true as a matter of practice. Further, it is often stated that coop interests, being personal property, are not subject to the restraint on alienation doctrine, and that is why the distinction exists.

In fact, in the 1980's a New York court found that coop interests were real property interests for purposes of the restraint on alienation doctrine and struck down a sale restriction in a coop development. A 1990's decision from a higher appellate court ignored that holding and concluded that sales of coop interests could be controlled by the coop board.

Coops argue that the more interdependent nature of the coop relationship is the real reason that they should have the authority to restrict resale. Every coop unit depends on every other coop unit to pay to support the general expenses of the master mortgage and other corporate expenses. Although condominium owners also pay maintenance assessments, they are not used to pay the master mortgage.

Comment 3: The editor is not ready to conclude finally that in his view the differences between coops and condominiums are sufficient to justify different judicial treatment of sale restrictions. He simply notes that this particular case, permitting restrictions on resale of special purpose units is not a wholesale abandonment of that distinction in New York.

CONSTITUTIONAL LAW; EQUAL PROTECTION: Exclusion of condominiums and cooperatives from the definition of "residential real property" in the property disclosure statutes violates the Equal Protection Clause. ***Goldman v. Fay, 797 N.Y.S.2d 731 (N.Y.City Civ.Ct. 2005),*** discussed under the heading: "Vendor/purchaser; Disclosure; Statutory Requirement."

CONSTITUTIONAL LAW; FREEDOM OF RELIGION; PUBLIC "ENTANGLEMENT:" City may transfer public right of way to private church for adequate consideration and thus negate the character of the right of way as a public form, even if the premises continues to be used by the public pursuant to the new private owner's permission. ***Utah Gospel Mission v. Salt Lake City Corp., 2005 WL 2421618 (10th Cir. 10/3/05)***, discussed under the heading: "Constitutional Law; Free Speech; Public Forum."

CONSTITUTIONAL LAW; FREEDOM OF RELIGION; ZONING; CHURCH DAY CARE CENTERS: Zoning authorities can refuse variance to church day care center notwithstanding First Amendment guarantees of freedom of religion. ***Grace United Methodist Church v. City of Cheyenne, 2005 WL 2746701 (10/25/05)***, discussed under the heading: "Zoning and Land Use; Religious Practices."

CONSTITUTIONAL LAW; FREE SPEECH; PUBLIC FORUM: City may transfer public right of way to private church for adequate consideration and thus negate the character of the right of way as a public form, even if the premises continues to be used by the public pursuant to the new private owner's permission. ***Utah Gospel Mission v. Salt Lake City Corp., 2005 WL 2421618 (10th Cir. 10/3/05)***

In 1999, the City of Salt Lake City sold a major downtown street to the Mormon Church, which installed in the street a an "ecclesiastical park" – a landscaped area pedestrian walkway lined with religious displays. The court in the current case characterizes the development as a "Plaza" "which the City hoped would promote downtown pedestrian traffic and stimulate business." The Church paid $8 million for the property and gave to the city an easement insuring that the property would always provide public pedestrian access between the two cross streets intersecting the property.

A group of non-Mormons who might have preferred that public property not be turned over to the Mormon Church for purposes of a one-sided religious display sued to establish that the public easement would include the opportunity for these groups to deliver their messages (sometimes antagonistic to Mormonism) in the same area. This lawsuit was successful, as reported in *First Unitarian Church of Salt Lake City v. Salt Lake City Corporation,* 308 F.3d 1114 (10th Cir. 2002), the DIRT DD for 5/27/03), where the court held that the public easement reserved in the private property could not be controlled in such a way as to prevent the exercise of Constitutional Free Speech rights, even if the parties to the easement agreement so contracted. This was because the easement area substituted for an existing public access and was carrying out the function of a public forum.

Not surprisingly, the City and the Mormon Church sought ways to accommodate the Church's desire to counter hostile speech exercises in the heart of its religious display area (which was adjacent to two immense Temples the Church maintained in the downtown neighborhood. The new plan involved the City's sale of the easement to the Church in exchange for $500,000 and the construction of a major recreational facility for the city. The court characterized the value the Church paid for the easement as "more than ten times its value." The City retained the right to maintain utilities under the ground and had a right of reentry if the Church failed to use the area as a "landscaped space," but there was no requirement that the Church use the property for an open pedestrian thoroughfare or that the city had any rights to maintain a thoroughfare.

Also not surprisingly, the same group of plaintiffs challenged this plan in court, arguing first that the property, having been a public forum, should be viewed as retaining its character as a public forum, even if it passes into private hands. It pointed to the U.S. Supreme Court precedent in Marsh v. Alabama, where the court held that a "company town" constituted a public form although in private hands. But the 10th Circuit noted that *Marsh* had been cut back in subsequent cases, perhaps most notable the *Lloyd Center* case, where the court held that a shopping center was not a public forum required to provide public speech rights (thus rejecting the *Pruneyard* doctrine which continues to be the law under state constitutions in about ten states (but not Utah.)

Plaintiffs argued that the motives of the City and Church in transferring the easement back to the city were transparent – to get to the same result of a downtown street being used as a permanent religious display. They claimed that if the property still functioned as a public thoroughfare, then it retained its public forum status even if there was no public easement. The court rejected this notion, concluding that the changes made by the Church clearly differentiated it from an ordinary public street (in fact it changed from vehicle access to pedestrian, among many other things) and therefore there could be no argument that the area was a public street under a different label. It did acknowledge, incidentally, that some authority involving situations in which cities attempted to maintain segregated public facilities by "privatizing" them did stand for the principle that where property continues to serve the same purpose, a "private owner" label will not alter its fundamental public character. But it saw the issues as different here, where the new use of the property, albeit still a right of way, was significantly different than before.

The court also rejected the argument that the retained right of reentry rendered the space a public forum. Recall that the right of entry was triggered if the Church altered the landscaped character of the space, not if it prohibited public use or access. Consequently, there could be no argument that the City was obtaining an easement in different clothing. A right of reentry itself, the court held, "does not constitute an actual estate," and that right, in and of itself, did not stamp the Church property as public in character. The court noted that a right of reentry is not a compensable interest in the event of a taking under the United States Constitution.

The fact that the property originally had been a public forum, the court held, did not irrevocably stamp it with that character. Otherwise public agencies would never be able to change their property or sell it for private use.

The court had even less difficulty with the claim that the arrangement violated the Establishment Clause because the government was engaged in supporting religious activity. It noted that the government argued that it was obtaining considerable public benefit from the installation of the "ecclesiastical park" in terms of increased pedestrian traffic and tourism in the downtown area, and that, in addition, the Church paid in excess of the fair value of the property it obtained.

The court did have to tap dance a little around the standard of *Lemon v. Kurtzman,* 403 U.S. 602 (1971), that "the court must consider not only whether the government is actually acting neutrally but also whether a reasonable observer, reasonably informed as to the relevant circumstances, would perceive the government to be acting neutrally." The court stated that the project satisfied the test. "The government is doing nothing to advance religion, but merely enables the LDS Church to advance itself." Right . . . . (Maybe the test is the "reasonable Mormon" test.)

A third possible bases for finding an Establishment Clause claim is that the government and the church are "excessively entangled." The court noted that in this case, following sale of the easement, the government and the church are less entangled than before. Of course, this is simply from the perspective of the instant moment, and does not take into account the entanglement that began when the entire "ecclesiastical park" notion was first introduced and negotiated through hours and hours of meetings and hearings and piles and piles of paperwork to carry out this unique activity. Is the fact that the entanglement already happened before it was challenged sufficient to avoid application of this test?

Comment: Life being what it is, we probably shouldn't worry too much about the City of Salt Lake City permitting this very important presence in its city to have a little leeway in promoting itself, even through the closure of streets and the installation of exhibits. Have other cities done less to facilitate (and even plan for and support) the construction of major cathedrals and synagogues? The editor is just having fun poking holes in the "pious" pronouncements of the court that something is going on that truly has a secular purpose. There's a religious purpose here – but at an institutional level that the editor is wiling to accept as "constructively secular."

CONSTITUTIONAL LAW; FREEDOM OF TRAVEL: State may constitutionally limit convicted child offenders from residing within 2000 feet of schools, even when the consequence might so narrow residential options as to constitute an effective banishment from the state. ***Doe v. Miller, 405 F. 3d 700 (8th Cir. 2005); petition to stay ruling pending appeal rejected 418 F. 3d 950 (8th Cir. 2005)***, discussed under the heading: "Constitutional Law; Restrictions on Residency."

CONSTITUTIONAL LAW; RESTRICTIONS ON RESIDENCY: State may constitutionally limit convicted child offenders from residing within 2000 feet of schools, even when the consequence might so narrow residential options as to constitute an effective banishment from the state. ***Doe v. Miller, 405 F. 3d 700 (8th Cir. 2005); petition to stay ruling pending appeal rejected 418 F. 3d 950 (8th Cir. 2005)***

According to the court, this case represents one of first impression in U.S. courts.

In 2002, in an effort to protect children in Iowa from the risk that convicted sex offenders may reoffend in locations close to their residences, the Iowa General Assembly passed, and the Governor of Iowa signed, a bill that prohibits a person convicted of certain sex offenses involving minors from residing within 2000 feet of a school or a registered child care facility. The district court declared the statute unconstitutional on several grounds and enjoined the Attorney General of Iowa and the ninety-nine county attorneys in Iowa from enforcing the prohibition.

On appeal, the Eighth Circuit Court of Appeals panel reversed. The court ruled unanimously that the residency restriction is not unconstitutional on its face. A majority of the panel further concluded that the statute does not amount to unconstitutional *ex post facto* punishment of persons who committed offenses prior to July 1, 2002, because the appellees have not established by the "clearest proof," as required by Supreme Court precedent, that the punitive effect of the statute overrides the General Assembly's legitimate intent to enact a nonpunitive, civil regulatory measure that protects health and safety.

It should be noted that the statute defines "sex offender" to include only persons found guilty of sexual crimes involving minors.

> "For purposes of this section, "person" means a person who has committed a criminal offense against a minor, or an aggravated offense, sexually violent offense, or other relevant offense that involved a minor."

The editor recalls that the statute was a response to a kidnaping and death of a minor child carried out by a neighbor who was a convicted sex offender.

The statute was promptly challenged in a class action brought by persons affected by the statute for themselves, other similarly situated, and other convicted sex offenders who might plan to move to Iowa. In reaching its decision that the statute was unconstitutional, the trial court first analyzed the scope of impact. It reviewed maps and heard testimony from a county attorney, and found that the restricted areas in many cities encompass the majority of the available housing in the city, thus leaving only limited areas within city limits available for sex offenders to establish a residence. In smaller towns, a single school or child care facility can cause all of the incorporated areas of the town to be off limits to sex offenders. The court found that unincorporated areas, small towns with no school or child care facility, and rural areas remained unrestricted, but that available housing in these areas is "not necessarily readily available."

After hearing the testimony experts from both sides concerning the possible effectiveness of the law in protecting children, and hearing from several individual plaintiffs, the district court declared that the statute was unconstitutional on several grounds: that it was an unconstitutional *ex post facto* law with respect to offenders who committed an offense prior to July 1, 2002; that it violated the plaintiffs' rights to avoid self-incrimination because, coupled with registration requirements elsewhere in the statute it required offenders to report their addresses even if those addresses were not in compliance its requirements; that it violated procedural due process rights of the plaintiffs; and that it violated the plaintiffs' rights under the doctrine of substantive due process, because it infringed fundamental rights to travel and to "privately choose how they want to conduct their family affairs," and was not narrowly tailored to serve a compelling state interest. Although the district court believed the law was punitive, the court rejected the plaintiffs' final argument that the law imposed cruel and unusual punishment in violation of the Eighth Amendment. Having found the statute unconstitutional, the district court issued a permanent injunction against enforcement.

As indicated, the appeals panel felt differently. It noted that the statute did not require individual determinations that persons subject to its ambit were themselves dangerous to children. The court concluded that the classification made by the statute was adequately clear and did not require an elaborate process of identifying those subject to its control.

The plaintiffs argued that the State faced a higher level of justification because the statute implicated "fundamental rights. The court rejected that claim as well:

> We do not believe that the residency restriction of § 692A.2A implicates any fundamental right of the Does that would trigger strict scrutiny of the statute. In evaluating this argument, it is important to consider the Supreme Court's admonition that " '[s]ubstantive due process' analysis must begin with a careful description of the asserted right, for '[t]he doctrine of judicial self-restraint requires us to exercise the utmost care whenever we are asked to break new ground in this field.' (Citations omitted). While the Court has not directed that an asserted right be defined at the most specific level of tradition supporting or denying the asserted right, the Does' characterization of a fundamental right to "personal choice regarding the family" is so general that it would trigger strict scrutiny of innumerable laws and ordinances that influence "personal choices" made by families on a daily basis. The Supreme Court's decision in Griswold and the plurality opinion in Moore did recognize unenumerated constitutional rights relating to personal choice in matters of marriage and family life, but they defined the recognized rights more narrowly, in terms of "intimate relation of husband and wife," Griswold, 381 U.S. at 482, 85 S.Ct. 1678, or "intrusive regulation" of "family living arrangements." Moore, 431 U.S. at 499, 97 S.Ct. 1932 (plurality opinion).

Although the plaintiffs cited several actual examples where the living restrictions would have prevented individuals from residing with family members, the court concluded that the impact on intimate family relationships was not "direct" and not of a character implicating fundamental rights.

Perhaps the greatest "fundamental rights" obstacle for the State was the argument that the statute violated the right to travel (remember that the consequence of the statute was that there were few places in Iowa where a sex offender could reside at all. The restriction on the right to travel had been a basis of the trial court's finding that the statute was unconstitutional. Here the court's analysis focused more on the effect of the statute, as the fundamental right clearly existed. But the court concluded, somewhat summarily that there was no unacceptable impact on the right to travel here. It stated, more or less, that the fact that a person could find few places to reside in Iowa didn't mean that a person could not travel there:

> "The Iowa statute imposes no obstacle to a sex offender's entry into Iowa, and it does not erect an "actual barrier to interstate movement.". . . There is "free ingress and regress to and from" Iowa for sex offenders, and the statute thus does not "directly impair the exercise of the right to free interstate movement." [citations omitted] Nor does the Iowa statute violate principles of equality by treating nonresidents who visit Iowa any differently than current residents, or by discriminating against citizens of other States who wish to establish residence in Iowa. We think that to recognize a fundamental right to interstate travel in a situation that does not involve any of these circumstances would extend the doctrine beyond the Supreme Court's pronouncements in this area. That the statute may deter some out-of-state residents from traveling to Iowa because the prospects for a convenient and affordable residence are less promising than elsewhere does not implicate a fundamental right recognized by the Court's right to travel jurisprudence."

Later:

> "The Iowa residency restriction does not prevent a sex offender from entering or leaving any part of the State, including areas within 2000 feet of a school or child care facility, and it does not erect any actual barrier to intrastate movement. . . . The Does also urge that we recognize a fundamental right 'to live where you want.' This ambitious articulation of a proposed unenumerated right calls to mind the Supreme Court's caution that we should proceed with restraint in the area of substantive due process, because '[b]y extending constitutional protection to an asserted right or liberty interest, we, to a great extent, place the matter outside the arena of public debate and legislative action.'"

Having concluded that there was no "fundamental right" challenged by the statute, the court had a much easier time dismissing plaintiffs' due process and equal protection attacks. The statute had a clear public purpose of protecting children from attacks by sexual criminals and the court concluded that the state's choice to pursue that purpose as it did was "rational."

The court also dealt quickly with the claim that the statute requires individuals to incriminate themselves, since they are already required to register their residences with local law enforcement, and now, by doing so, might admit that they are in violation of the residency restriction. The court concluded that the argument was "misdirected and premature," as there was no evidence that Iowa would treat a registration as an immediate admission of a violation of the statute.

The judicial panel split on whether the provision of the statute reaching back to restrict the conduct of persons convicted of sex crimes subsequent to July 1, 2002 created an *ex post facto* law, adding additional punishment to crimes already charged and sentenced. The majority ruled that the statute here had a civil, not a punitive purpose, and that this was sufficient to avoid the claim that it was an unconstitutional *ex post facto* law. But there was still the question of whether the statute had a punitive effect in that it worked a form of "banishment" on convicted offenders. The majority ruled that the impact of the statute did not extend that far:

> "While banishment of course involves an extreme form of residency restriction, we ultimately do not accept the analogy between the traditional means of punishment and the Iowa statute. Unlike banishment, § 692A.2A restricts only where offenders may reside. It does not "expel" the offenders from their communities or prohibit them from accessing areas near schools or child care facilities for employment, to conduct commercial transactions, or for any purpose other than establishing a residence. With respect to many offenders, the statute does not even require a change of residence: the Iowa General Assembly included a grandfather provision that permits sex offenders to maintain a residence that was established prior to July 1, 2002, even if that residence is within 2000 feet of a school or child care facility . . . ."

Although the court acknowledged that there was some evidence that the statute would present a severe restriction on living accommodations for some individuals, the court concluded that the state's only burden was to show that this restriction was rationally consistent with the civil purpose of the enactment. The court cited evidence in the record that convicted sex offenders generally are not fully deterred by punishment and cannot be cured. Consequently, it was rationale for the state to protect its children by separating them as a class from places where children congregated.

It was on this point, however, that the dissent parted company with the other two judges. The dissenting judge concluded that the statute swept too broadly, and imposed a "banishment" result on persons who did not present the high level of threat to children that the statute was designed to address:

> "There is no doubt a class of offenders that is at risk to re-offend and for whom such a restriction is reasonable. However, the restriction also applies to John Doe II, who pleaded guilty to third degree sexual abuse for having consensual sex with a fifteen-year-old girl when he was twenty years old. The restriction applies to John Doe VII, who was convicted of statutory rape under Kansas law. His actions which gave rise to this conviction would not have been criminal in Iowa. The restriction applies also to John Doe XIV, who pleaded guilty to a serious misdemeanor charge in 1995 after he exposed himself at a party at which a thirteen-year-old girl was present. John Doe XIV was nineteen at the time of his offense. The actions of these and other plaintiffs are serious, and, at least in most cases, illegal in this state. However, the severity of residency restriction, the fact that it is applied to all offenders identically, and the fact that it will be enforced for the rest of the offenders' lives, makes the residency restriction excessive.
>
> In my view, four factors weigh in favor of finding the statute punitive, while only one weighs in favor of finding the statute nonpunitive. The analysis leads me to the conclusion that the residency restriction is punitive. . . . [T]he imposition of the residency requirement " 'changes the punishment, and inflicts a greater punishment, than the law annexed to the crime, when committed. . . .'"

Comment 1: One is tempted to say that this decision will not be reviewed by the high Court and that, whatever the merits of the technical arguments here, the society will not accept a court's meddling with the way that society protects its children from sex offenders. Yet, as prior courts have pointed out many times, the true test of the extent of our liberties is whether they extend to those least valued by society. We are taught constantly that to permit overreaching by government in one case involving very unpopular victims invites similar overreaching to reach only somewhat unpopular victims, and eventually to reach everyone who falls outside the majority viewpoint. If an eighteen year old who had sex with her fifteen year old boyfriend and was convicted of statutory rape can effectively be banned from residing most places in Iowa on the argument that she poses a threat to Iowa's children, can the state similarly restrict anyone convicted of selling liquor to minors? All persons convicted of possessing child pornograph? All registered Libertarians? All registered Democrats?

Comment 2: The decision to review this case *en banc* also was a split decision, with five judges voting to take the case. There was also a split on whether the decision ought to be stayed pending Supreme Court review. Ultimately, the court concluded that review at this stage was unlikely because the issue was one of first impression on which there had been no disagreement among the circuits or between the state court and federal courts. (The Iowa Supreme Court reached a similar result in a parallel challenge to the statute.)

Clearly many judges are troubled by the implications of this case, and so is the editor. Perhaps the theory of the statute is acceptable, but the consequences of it are troubling, and the editor believes that much more analysis is required to conclude that the statute is properly drawn and that alternatives have been fully weighed.

Comment 3: Is this a "property law" case or a "sex offender case?" The editor obviously believes that the principles here could reach far beyond the case of sex offenders, and it is worth contemplating whether our society should be able to restrict specially any individual's choice of residence except in extreme circumstances.

CONSTRUCTION; CONTRACTOR LIABILITY; STATUTE OF LIMITATIONS; STUCCO: In an action alleging breach of contract and negligent installation of synthetic stucco, the six-year statute of limitations on a breach of contract claim begins to run on the date the homeowners purchase a house, even if the house is substantially completed before title is conveyed to them have knowledge. ***Skully v. First Magnolia Homes, 614 SE 2d 43 (Ga, 2005).***

The Court of Appeals had held that damage to property arising out of faulty construction is considered to occur on the date of the project's "substantial completion, i.e. when the certificate of occupancy is issued." Because the house at issue here had already been substantially completed when the Plaintiffs entered into the purchase and sale agreement, the Court of Appeals held that the statute of limitations began running when the agreement was executed.

The Supreme Court of Georgia reversed. It noted that the ordinary rule for breach of contract damages against a contract related to work done on a building is the date of substantial completion, because it is assumed that at that time the owner is in a position to identify defects. But it noted that Georgia courts have noted an exception when the work is not done to property already owned by the plaintiff, but rather when the property is still in title to the contractor. In such cases, the court stated, the date of completion is not a relevant date for ascertaining whether it is reasonable for the owner to identify the defects.

But rather than follow the Court of Appeals conclusion that the date of contract of sale to the buyer should apply, the court held held that if a new house is defectively constructed by an owner/builder for the purpose of sale, the applicable period of limitations for damage to realty begins to run at the time of the closing of the initial sale of the improved property, regardless of the date of 'substantial completion." In light of that formulation, the plaintiffs filed their lawsuit two days prior to the running of the statute.

At to the action for negligence, however, the court agreed with the Court of Appeals that the action begins to run at the time that the plaintiff reasonably should have become aware of th potential claim (presumably when it discovered the defect.).) Note that the statute of limitations on negligence is shorter – four years vs. six years on the contract claim. The result was in this case the plaintiffs were out of look on their negligence claim, but made their contract claim by two days.

Comment 1: Is the court reaching too far to protect the home buyer? If the principle is to establish a time when the homebuyer should become aware of defects in the property, wouldn't it be appropriate to assume that the homebuyer has examined the property before agreeing to buy it, rather than to assume that it won't make such an inspection until after closing?

Of course, in many real estate contracts there is a "due diligence" period following contract, and the conclusion of that period probably is the time that the contract truly becomes binding and that is likely the best time to use. The court's use of the closing date is meaningless in terms of the stated purpose of the choice for the date the statute begins to run.

Comment 2: In this case, the buyers in fact did not identify problems until well after they had closed on the home. They learned of potential defects in the products used from talking to friends and neighbors who owned similar houses. But a neighbor, who was a real estate broker, told them that the problems were exaggerated. Consequently, they waited a bit longer to get a full inspection, and the statute of limitations on negligence ran in the meantime. Hmmmm. Good Samaritan or "officious intermeddler?"

CONSTRUCTION; PERSONAL GUARANTY: A personal guaranty on an open account for construction materials failed to sufficiently identify the principal debtor by name where there was no entity identified as "Applicant" in the credit application, and therefore was unenforceable, despite clear intent of the parties. ***McDonald v. Ferguson Enterprises, Inc., 2005 WL 1531070 (Ga.App., June 29, 2005).***

Plaintiff claimed Defendant was liable pursuant to a personal guaranty agreement for "all sums owed by his company" on an open account for construction materials. While the "Terms Section" of the credit application immediately above the personal guaranty section identified the applicant for credit as the "undersigned applicant", the two undersigned signatories were specifically identified as "Witness" and "Owner/Officer". No one was identified as "Applicant". On that basis, the Court of Appeals of Georgia applied the Statute of Frauds and barred enforcement of the guaranty, despite the obvious intent of the parties.

CONSTRUCTION; CONTRACTOR LIABILITY; STATUTE OF REPOSE: Where a proper lawsuit is brought within the ten year construction claim repose period, a previously unknown, though functionally identified, designer or builder may be named after expiration of the period of repose. ***Greczyn v. Colgate-Palmolive, 183 N.J. 5, 869 A.2d 866 (2005); March 21, 2005.***

An accident victim sued a "John Doe" designer after slipping and falling on a staircase that had been built nearly nine years before the accident. A year after New Jersey's construction ten-year statute of repose period had passed, the victim substituted the fictitious name of the staircase designer for its real name. The designer claimed that the victim could not sue it since it was not named until after the ten-year period had passed.

The Appellate Division disagreed with the designer, holding that despite not calling the designer by its name, the victim's complaint satisfied the requirements of New Jersey law since it fully identified the "persons" being sued by their function, and so long as the victim was diligent in seeking the designer's true name, the victim was permitted to name the designer after the statute of repose period had passed. Additionally, the suit was permitted since the victim was both injured and filed her suit within the ten-year repose period. Finally, the Court concluded that only when the elements of well- timed filing and due diligence in seeking a fictitious party's name are met, may this type of suit be brought, thus making finite and restricted the designer's potential exposure to liability.

Comment: This strikes the editor as a sensible and valuable interpretation of this statute, which, after all, extends to builders protection that is not available to many other tortfeasors. But builder clients should be warned of the possibilities.

CONSTRUCTION LAW; CONTRACTOR LIABILITY; STATUTE OF REPOSE: The Tenth Circuit, applying Oklahoma law, holds that machinery weighing between 60 and 80 tons is not an improvement to real property, and therefore the manufacturer is not sheltered under Oklahoma's 10-year statute of repose for liability based on improvements to real property. ***Durham v. Herbert Olbrich GMBH & Co., 404 F.3d 1249 (10th Cir. 2005).***

Plaintiff sued the manufacturer of a vinyl flooring production line (installed in 1987), alleging design flaws. The Federal District Court found that the production line qualified as an improvement to real property, which made Oklahoma's 10-year statute of repose applicable, and that application led to summary judgment in the manufacturer's favor. The Tenth Circuit reversed the decision. The Tenth Circuit based its determination of the production line's status as personal property on several factors: 1) the item's tax treatment; 2) the ownership of the item; 3) the permanence of the improvement; 4) whether the improvement enhances the value of the realty; and 5) the party's intent in regards to improving the realty. The Tenth Circuit found that the Plaintiff's treatment of the production equipment as personal property for tax purposes supported the Plaintiff's argument that the 10-year statute for real property had no application in this case, despite the mass of the production line, and reversed the District Court's grant of summary judgment for the manufacturer.

EASEMENTS; CREATION; IMPLICATION: An implied easement requires a presumption of intent, and where deed to the adjoining properties contracted a deed with an express easement, destruction of that access through septic work that had been contemplated at execution of the deed does not give rise to a different, implied easement. ***Zotos v. Armstrong, 828 N.E.2d 551 (Mass. App. Ct. 2005).***

In 1995, French subdivided a property into two parcels. Zotos purchased one lot, which included French's home, and Armstrong ultimately acquired the other lot, which was undeveloped at time of trial. The subdivision plan depicted access to the properties from an adjoining road via an easement on the southern end of the properties (the "Access Easement"). A semi-circular driveway that crossed both parcels gave each property direct access to the Access Easement, and Zotos' deed established an express easement over the Access Easement. Prior to the subdivision, the entire semi-circular road was used by French.

Zotos' original closing was scheduled for January, 1996, but delayed until May 30 due to septic issues. Upon the eventual closing, $20,000 was escrowed pending the installation of a new septic system. Nancy Zotos had picked up the plans for the new septic system from the town's director of public health and delivered them to her attorney, but she claimed she did not review them. The construction of the new septic system started on May 29, one day before Zotos closed. The installation of the new septic system blocked direct access from the Access Easement to Zotos' portion of the driveway. French, at least, was fully aware that the leach field of the septic system would make it impossible to use the existing portion of the semi circular road on Zotos' property to get to the Access Easement, and the original septic plans had called for a new driveway extension (apparently to be built by French) to restore this access. The extension was never constructed, and the court suggest strongly that French had an obligation to build it, but that issue was not before the court here.

Zotos began using portion of the semi circular driveway over the other parcel to traverse to and from the Access Easement. However, French eventually posted "no trespassing" signs and attempted to prevent such use. Zotos then brought suit against French (Armstrong was substituted after he took possession of the other parcel) seeking declaration of an easement by implication or by necessity.

The Land Court found that French and prior owners had used the driveway in same fashion which Zotos now sought for sixty years, and that since some form of access must have been intended, and since continued use by Zotos was reasonably necessary for access, an implied easement should be granted. Armstrong, having been substituted in the place of French, appealed.

The Appeals Court, citing *Hurley v. Guzzi*, 103 N.E.2d (Mass. 1952), noted that an implied easement arises from a combination of necessity and the presumed intention of the parties. The court noted that where an express easement has been granted, silence with respect to any other easement tends by implication to be significant in proving the intent not to grant such an easement. Here, the Access Easement was expressly created to reach the main road. Additionally, Zotos had actual knowledge of the septic installation plan, and should have been aware of the consequences detailed therein. The plan shows that a new driveway would need to be created on the property, and failure to obtain an express easement over the second parcel to use the existing driveway established a lack of intent to create such access. The court also noted that any contractual claim as to the creation of the second driveway per the plan was not at issue in the appeal. The judgment was reversed, and a new judgment ordered declaring that no easement by implication existed.

Comment 1: The case is interesting because of the proper focus on the notion that an implied easement does not arise directly from facts, but only from the inference drawn from the facts that the parties likely intended that an easement exist. It is sometimes overlooked that the presence of a preexisting quasi easement is only evidence that the parties intended that the easement continue in use, and hardly not conclusive.

This is less true of an easement by pure necessity, which presumably was not at issue here. Based upon what the court tells us, the evidence does suggest that the parties did not intend that the other driveway continue in use, but note that the trier of fact found that there was an implied easement.

Comment 2: Note also that it may have been French who failed to follow through to provide the correct access improvements, so it is interesting that French and his successor in interest, who might have had actual or constructive notice of Zolo's use of the old driveway, gets away with ducking the easement while simultaneously failing to follow through on providing the alternate access. The court simply writes that off by saying that this dispute is not at issue in the case.

The editor might have ruled that French and anyone taking through him with knowledge of Zolo's claim is estopped from relying on the existence of a roadway that French never built as establishing that there was no implied easement intended for Zolos over the old road. In other words, Zolos gets the old road until French provides the new one. But that's just me . .

EASEMENTS; CREATION; IMPLICATION; PUBLIC LANDS: Even if a landowner establishes the elements of an easement by necessity or implication, the landowner is not entitled to an easement over the State's wilderness property absent a permit. ***Thomas Gang, Inc. v. State*, 797 N.Y.S.2d 583 (A.D. 3 Dept. 2005).** New York State appropriated a parcel of land, thereby causing the parcel to its south to become landlocked. The plaintiff subsequently bought the landlocked parcel.

When the State refused the plaintiff's application for temporary revocable permits to traverse the State land, plaintiff brought suit. When the State takes land through eminent domain, it takes it in fee simple absolute, extinguishing all easements, and, further, when the State takes land and designates it as forest preserve, that land, by the N.Y Constitution, cannot be encumbered with an easement. Therefore, even though the plaintiff established the elements of easement by implication and, arguably, easement by necessity, the Court held that the plaintiff was not entitled to an easement over the State's land.

EASEMENTS; CREATION; PRESCRIPTION. Prescriptive easements for discharge of sewage waste are not granted in Ohio. ***Morris v. Andros, 815 N.E.2d 1147 (Ohio App. 9 Dist. 2004).***

Morris filed a declaratory judgment action on August 10, 2001 against Andros for ejectment, trespass, and nuisance abatement. Morris' complaint alleged that Andros had constructed without Morris' permission a sewer and septic line that protruded through Morris' property and deposited septic waste into a ravine on Morris' property. Andros asserted, among other counterclaims, that he had satisfied the requirements necessary to acquired a prescriptive easement by way of tacking. The trial court bifurcated the issues and scheduled a hearing to determine whether an easement by prescription existed.

The trial court then held that Andros was not entitled to take title by adverse possession but was entitled to a prescriptive easement for the portion of his septic system residing and discharging on Morris' property. Reviewing *de novo*, the Ohio Court of Appeals held that the trial court erred as a matter of law in granting Andros a prescriptive easement, citing *Vian v. Sheffield Bldg. & Dev. Co.*, 88 N.E.2d 410 (Ohio App. 9 Dist. 1948), for the principle that one may not obtain by prescription, or otherwise than by purchase, a right to cast sewage upon the land of another without his consent. That Andros was cited for Health Code violations for not possessing any recorded easement for the discharge was further proof to the court that no express easement existed. The trial court's denial of Andros' claim of adverse possession was affirmed. The judgment of the trial court granting Andros a prescriptive easement was reversed and cause remanded.

EASEMENTS; CREATION; PRESCRIPTION: In New Jersey, the thirty year period required for obtaining adverse possession is the same period required to obtain a prescriptive easement regardless of whether the land is developed or uncultivated. ***Randolph Town Center, L.P. v. County of Morris, 374 N.J. Super. 448, 864 A.2d 1191 (App. Div. 2005); February 1, 2005.***

A real estate development company sued a municipality after the municipality began to pump out water through a culvert onto property owned by the company; the company planned to develop the property into a shopping center and the water drainage created wetlands which made any commercial development of the property either hard or impossible.

The municipality defended its conduct by claiming that it obtained a prescriptive easement to use the culvert, claiming it had done so for the twenty-year period needed to establish a prescriptive easement. The lower court subsequently ruled in the municipality's favor. The company appealed, arguing that the lower court had utilized an incorrect time period for obtaining prescription.

The Appellate Division reversed, holding that the thirty-year period required for obtaining adverse possession is the same as the period required to obtain a prescriptive easement, and the lower court was in error when it distinguished between the two. The Court likewise held that this required time period applies to all types of property, and not just to uncultivated land or to woodlands. In a footnote, the Court also held that there was no support for the company's additional argument that a municipality cannot obtain a prescriptive easement.

EASEMENTS: CREATION; PRESCRIPTION; GOVERNMENTAL ENTITIES: A governmental entity can acquire a prescriptive easement to a roadway; and once such an easement is acquired, a later permissive allowance of use will not alter or destroy it. ***Wood v. Village of Kipton, 828 N.E.2d 173 (Ohio App. 2005).***

Landowners filed suit against the village of Kipton (the "Village") seeking to quiet title to a paved road that ran through property the Landowners owned. The Village claimed the road as a section of public roadway, or in the alternative that a prescriptive easement had been obtained. The County Court of Common Pleas granted declaratory judgment and quieted title, granting a permanent enjoinment against public use of the road. The Village appealed, asserting that the trial court had improperly excluded county records dating to 1861 which purported to show the roadway had been established as a public road. The Appeals Court granted the appeal, allowing the admission of the documents, and remanded to the trial court. The trial court again ruled for the Landowners against the Village. The Village again appealed on several grounds, and the Appeals Court sustained the Village's assertion that as a matter of law, a prescriptive easement had been established. Citing *State ex. rel. AAA Investments v. Columbus*, 478 N.E.2d 773 (Ohio St. 1985), for the proposition that "governmental entities may acquire title to land by adverse possession," the court noted that the elements for a prescriptive easement are identical: use that is open, notorious, adverse, continuous, and exceeds the statutory temporal requirement. Where testimony showed that the town had used the road for at least fifty years, the town had paved and plowed the road, and no permission had been given for its use, a prescriptive easement had been established as a matter of law. This was held true despite the fact that use of the road became permissive in 1979 because the prescriptive easement had already been established at that time. Acquiescence to use will not negate a claim for an earlier prescriptive easement. The trial court's judgment was reversed, and new judgment was entered for the Village.

EASEMENTS; DUTIES OF SERVIENT TENANT: Holder of pipeline easement can enjoin servient owner from permitting operation of four wheel drive recreational vehicles in easement area where evidence shows that such operation has led to erosion of the soil covering the pipes, thus creating a danger of explosion or fire from materials the pipes carry. ***Still v. Eastman Chemical Co., No. 06-04-001224-CV (Tex. App. 2005)***

Eastman had various easements to run pipelines for chemical products under Still's land. It buried some of its pipes at depths of 44 to 60 inches. Still operated an all terrain vehicle park on the surface of the land, involving driving by groups of recreational vehicle drivers in organizations with such names as Rabbit Creek Mountain Mud Blast and East Texas All-Terrain Monsters.

Pipeline inspects observed that there was rutting and consequent erosion in the area of the easements, in some cases reducing the surface area over its pipelines to less than 24 inches, a depth deemed unsafe by federal authorities regulating such pipeline activities. Eastman expressed a concern of fire or explosion resulting from the breach of the pipelines as a consequence of their being so near the surface.

There was scant evidence that Still had in fact encouraged or directed his customers to drive in the area of the pipelines. Nevertheless, the court upheld the trial court's issuance of an injunction prohibiting Still from "permitting vehicles to continue using the pipeline easements in a way that caused such erosion or rutting."

Comment 1: The result is not surprising and consistent with law. In fact, the easement likely was more moderate than it might have been, since it apparently permits Still, if possible, to continue to permit operation of all terrain vehicles on his land, so long as he regulates the activity in such as way as to prohibit rutting over the pipelines. Of course, there is no guarantee that any regulation would be followed or that compliance could be policed.

Comment 2: Although the decision does not really advance the law, the editor selected it because it reflects the absolute protection typically given to the uses established by an easement right. Easement interference cases are not nuisance cases. There is no "reasonable balance" to evaluate. The parties have set the balance when they agreed to the easement. From the standpoint of the servient owner, an easement is more than permission to go on one's land, it is an undertaking to avoid activities on the land that would interfere at all (not just "unreasonably") with the dominant use.

Comment 3: Of course Eastman could have maintained the coverage over its pipelines by sending out crews regularly to restore it. Or it could have installed protective casings over the lines or just buried them deeper. None of this seemed to matter. It was entitled to conduct its use and expect the servient owner to protect it from interference.

Of course, if the pipeline use was of a character radically different from "ordinary" pipeline activities, the court might have concluded that this use was not one of those uses intended by the parties to the easement. But that wasn't about to happen in this part of East Texas.

EASEMENTS; SCOPE; INTERFERENCE; PUBLIC RIGHT OF WAY: A easement granted to a City "for purposes of relocating, establishing, opening and improving Dan Hoey Road" cannot be used by an abutting owner to develop access roads, utilities, sidewalks, landscaping and other facilities from the road to the owner's development, even when the City consents. ***Blackhawk Dev. Corp. v. Village of Dexter, 700 N.W. 2d 364 (Mich. 2005)***

The city, after first contemplating ownership of the land in question by eminent domain, eventually entered into a contract with Trust, the owner and the plaintiff in this action, to acquire an easement. Apparently significant to the court was the fact that the contract provided that the easement was to be for "public roadway purposes . . . ," even though the actual easement grant document described the purpose of the easement as set forth above in the caption – for "relocating, establishing, opening and improving" an identified road. In the end, the road was moved some distance to the south and improved with a hard surface.

The Trust then sold to Kingsley what the court describes as "the burdened parcel," who built a commercial project on the property, but left undeveloped the area of the easement not already committed to the roadway. (Although the court refers to Kingsley's property as "the burdened property," apparently the Trust must have retained some property that was subject to the easement – else it would hardly have standing to be objecting to the use of the easement, as it did here.)

Kingsley then acquired additional land that had been abutting the old road, but now was separated from the new road by the balance of the undeveloped easement area. He proposed to expand his commercial development, using portions of the easement area for constructing access drives, building a pond (characterized by the dissent as nothing more than a "drainage facility," installing sewer and other utility facilities, installing lights, and making certain other developments. After some negotiation back and forth, the City consented to Kingsley's proposal. Any developments on the parcel not directly related to access to the road would be dedicated to the City as public improvements. There is some argument that a City employee erred in concluding that the proposal had to be granted in part because Kingsley would otherwise have been landlocked, but it is not clear that the City, even at time of trial, was in opposition to Kingsley's proposal.

The party who did oppose Kingsley's use of the easement area for this purpose was the Trust, that had initially granted the easement to the City and then sold the burdened parcel to Kingsley. It argued that the use of the property for utilities and various other public improvements was not use of the property for expansion and improvement of a public road. It even argued that using the easement property for access roads to the new roadway (originally, remember, abutting Kingsley's property) was not a "public road use."

The court stated the principles that the conveyance of an easement gives the grantee all rights incident or necessary to the reasonable and proper enjoyment of the easement, but also that the use made by the easement owner must be reasonably necessary and convenient to the proper enjoyment of the easement, with as little burden as possible to the land." The court saw these questions as two sides of the same issue – a use that is not reasonably incident or necessary to the easement purpose necessarily overburdens the servient estate. But even if the actions are reasonably necessary, the may not be permitted if they **unreasonably burden the servient estate anyway.**

Much of the attention of the parties focus ed on whether the challenged activities were "improvements," since arguably they did not involve relocating the roadway – a project that was completed. The court completed that the various improvements did nothing to improve Dan Hoey Road itself, but rather improved the adjacent property or the access ways that were to be built. Even though the improvements were to be dedicated to the public as public improvements, the court contended, this made no difference. Even if the City built them, the majority stated, it still would analyze whether they constituted improvements to the public Road, and the same analysis would occur. [The dissent strongly disputes this conclusion.]

The dissent also argued that an access road is a use of the road. But the majority concluded that these private access roads did not benefit the road, but benefitted the owner of the adjacent property.

The court then indulges in a restatement of some principles dear to the editor's heart when it states that a party may not unilaterally alter an easement. It also states that the language of the original agreement, discussing the purpose of the easement to be "a public roadway" should not be taken into account, since the parties elected to use more precise language [in its view} in the easement document itself. The court also rejected the notion that the interpretation of the scope of the easement ought to be looser because the easement was held by a public entity. Although it had early acknowledged that a right of way for a public road implicitly included the right to lay utilities in the road, it concluded that this was because such use was inherent in the nature of the public road, and not because a public agency owned the easement.

Comment 1: The court is rather vague about some of the intended improvements, and we must set aside completely its statement that Kingsley got title to the "burdened parcel," since the whole case makes no sense if that were literally true.

But making due allowances for these issues, the editor still believes that the decision is wrong. First, it is wrong in the fundamental premise that a the dominant owner of an easement must limit its activities to only those minimally necessary to achieve its purposes and, even then must alter its behavior so as not to interfere with the servient tenant's interests. This is not how the balance generally is perceived. An easement is a grant of use rights, and the dominant tenant has a reasonable right to carry out those rights. If these activities restrict the usability of the parcel for the servient tenant – normally that's not considered particularly significant. Perhaps nuisance standards apply, and if that's all the court means by "reasonably" limiting the dominant activity, that would be all right. But the whole sense of the court is that an easement usage must be as minimal as possible to protect the expectations of the servient owner. This is not the editor's view of the balance struck in other cases.

Comment 2: An example of that approach is the court's insistence that even an access road reconnecting the parcel that was once adjacent to the old road is not part of the relocation of the road. That strikes the editor as excessively narrow. In this case, the City was grudgingly going along with Kingsley's case, but clearly, at least based upon the testimony analyzed by the court, the city did not go overboard embracing Kingsley's purposes as congruent with public policy.

Justice Kelly's dissenting opinion is worth reading. Not only do her views correspond to those of the editor (always a good start), they stress that the whole easement area was acquired in perpetuity by the city – much more than that necessary, and consequently, Justice Kelly argues, the parties must have anticipated that something would happen on the rest of the property, and not just within the roadbed.

ENVIRONMENTAL LAW; ENVIRONMENTAL IMPACT; RETAIL DEVELOPMENT: California courts wrestle with question of environmental impact of supercenter. ***Maintain Our Desert Environment v. Town of Apple Valley, 124 Cal. App. 4th 430, 15 Cal. Rptr. 3d 322 (2004); Bakersfield Citizens for Local Control v. City of Bakersfield, 22 Cal. Rptr. 3d 203 (Cal. App. 2004)***

As some readers are aware, a major political battle is being waged in some parts of America between Wal Mart and a group of political interests, including community activists and union groups, who are hostile to Wal Mart essentially because its business practices have been so effective that they have had massive social consequences. The motives for the "antis" range from traffic concerns and other environmental impacts to concerns about wages and benefits, impact on competing stores and, for that matter competing development, contribution to urban sprawl when Wal Mart abandons a location and no other retailer can afford to occupy the deserted space, etc. etc.

California has one of the most involved land use processes in the nation, with a requirement for an elaborate environmental impact report layered upon any major land use decision. Recently, the "antis" have attempted to use the environmental impact report process to delay or otherwise hinder Wal Mart from locating facilities in various California neighborhoods. The two above cited cases are the latest appellate reports stemming from this continuing gunfight.

The first case, *Maintain Our Desert Environment* (yes – the felicitously named Apple Valley is indeed a desert community), dealt with a land use request to construct a 1.2 million square foot distribution center. The local planning authorities identified the project as having potentially significant environmental impact, commissioned a study and a report and, when all was said and done, approved the project after considering the report.

Shortly thereafter, plaintiffs, joined by the California Attorney General, sued to set aside the approval because the environmental report was flawed in that it did not identify that the likely user of the distribution center was Wal Mart. The issue was joined as to whether the identity of a tenant of such a distribution center was a central factor to be considered in the preparation of an environmental impact statement. The plaintiff argued that Wal Mart's identity should have been disclosed in the report and in notices concerning the hearing on the report. The city concluded that this was not required, and the court of appeals here agreed.

> "So long as the project is approved, [the California Environmental Quality Act] has no concern about who uses it. If CEQA compliance required the identification of the project end

> user, a new EIR would need to be considered every time property was sold or a different tenant moved into a building, regardless of the use to which the property was to be put."

The plaintiffs argued that, by disguising the identity of Wal Mart, many avid opponents of Wal Mart projects were not given the opportunity to protest at the hearings. But the court concluded that any basis for opposing the project related to the fact that Wal Mart was a tenant would entirely speculative and inadmissable in court.

> "The crux of the issue is that the project itself, and therefore its environmental impact, is identical regardless of who will operate it. The only possible reasons for the public to object to accepting Wal Mart but not a competitor under these circumstances have noting whatsoever to do with the aims and purposes of CEQA."

The court acknowledged that identity of an end user might be relevant if it had an unsatisfactory environmental record elsewhere in the country. But plaintiffs here had not tried to justify their opposition to Wal Mart by reference to Wal Mart's environmental history. The plaintiffs also argued that it might be important to name the end use because the community deserves to know whether the applicant end user will have the wherewithal to deal with environmental issues as they come up. The court ridiculed that notion, pointing out that land use decisions ought not to be made on the basis of relative wealth.

The sweep of the *Maintain Our Desert Environment* case is limited somewhat by the *Bakersfield* case, decided a few months later. *Bakersfield* made plain that, whatever might be the case with a distribution center, it certainly is appropriate to identify the end user of a project if the proposal is for a "supercenter." The court defined a "supercenter" as the combination of a traditional Wal Mart discount store with a full-size grocery store. The opinion is somewhat vague as to whether a "supercenter" in the view of the court is always a Wal Mart, or whether some other operator could be viewed as a "supercenter" operator if it combined discount and grocery operations. Although the court was very careful to indicate that the economic battles Wal Mart has with unions is not relevant to the environmental impacts addressed in an EIR, it concludes that other impacts considerations of the impact of a "supercenter" store operation make it vital that the EIR identify the proposed operators of the center. California courts ought not to approve EIR's for shopping centers with "stealth" supercenter.

In *Bakersfield,* there were proposals for two regional shopping centers, only about 3.6 miles apart. One developer did list the future tenants, including a Wal Mart supercenter, the other did not identify any tenants, stating that no tenants had as yet been selected. In fact the developers of the other center also were negotiating with Wal Mart to locate a supercenter there. (Two such centers 3.6 miles apart??? Golly.)

The planning authorities concluded that both proposed projects posed a risk of significant adverse environmental impacts, and ordered EIRs. Both EIR's identified significant adverse impacts, but the agencies found the impacts to be within an acceptable range and approved each project. Opponents then challenged both EIR's in court, seeking an injunction halting construction. By the time of the lawsuit, the fact that Wal Mart had a supercenter going into both locations was known, and the court found the EIR's deficient in that one did not identify the Wal Mart proposal and that neither took into account the impact of a combination of two supercenters so close together, which the court suggested could contribute to "urban decay." This decay would result, the court concluded, both from the closing of a nearby Wal Mart to be replaced by a supercenter and the impact on other "general retail businesses" in the area. The court decertified the EIR's. It refused to enjoy all construction on the two regional shopping centers, but did enjoin construction of the supercenters at both locations.

The appeals court started off the discussion with a general disclaimer, which strikes the editor as somewhat unusual for a court at this level, so he has quoted it below:

> "At the outset, it is necessary to explicitly reject certain philosophical and sociological beliefs that some of the parties have vigorously expressed. For the record, we do not endorse BCLC's elitist premise that so-called "big box" retailers are undesirable in a community and are inherently inferior to smaller merchants, nor do we affirm its view that Wal-Mart, Inc. (Wal-Mart), is a destructive force that threatens the viability of local communities. Wal-Mart is not a named party in these actions and we rebuff [plaintiff's] transparent attempt to demonize this corporation. We do not know whether Wal-

> Mart's entry into a geographic region or expansion of operations within a region is desirable for local communities. Similarly, we do not know whether Wal-Mart is a "good" or a "bad" employer. We offer no comment on Wal-Mart's alleged miserly compensation and benefit package because [plaintiff] did not link the asserted low wages and absence of affordable health insurance coverage to direct or indirect adverse environmental consequences.
>
> Likewise, we will not dignify with extended comment [defendant's] complaint that [plaintiff] is just a "front" for a grocery worker's union whose disgruntled members feel threatened by nonunionized Wal-Mart's entry into the grocery business. As will be explained, [plaintiff] has standing to pursue this litigation and it exhausted its administrative remedies. This is sufficient. We do not know whether Wal-Mart adversely affects the strength of organized labor and we have not considered this question.
>
> In sum, we have no underlying ideological agenda and have strictly adhered to the accepted principle that the judicial system has a narrow role in land use battles that are fought through CEQA actions. "The only role for this court in reviewing an EIR is to ensure that the public and responsible officials are adequately informed ' "of the environmental consequences of their decisions before they are made." ' "

We then come to the elaborate tap dance by which the court, having denied an interest in Wal Mart's economic and social impacts, then reached the conclusion that indeed economic such issues are environmental issues and need to be evaluated. The court first states that the EIR process requires the identification of "both primary (direct) and 'reasonably foreseeable' secondary (indirect) consequences be considered in determining the significance of a project's environmental effect." Further, the court noted that state guidelines for the CEQA state that "the economic or social effects of proposed projects are outside the Act's purview." But then the court winds round again: "[I]f the forecasted economic or social effects of a proposed project directly or indirectly will lead to adverse physical changes in the environment, then CEQA requires disclosure and analysis of these resulting physical impacts."

The court cited prior California cases, included some of its own decisions, supporting the conclusion that closure of competing businesses as a consequence of competition from a new business brought in by a real estate development project was an "adverse environmental" effect, at least if the competing businesses were not likely to be replaced by other businesses. The only interruption in the steady drumbeat of cases moving toward judicial economic policy making through EIR's was a case in which a court refused to require analysis of the impact of a Border's book store on existing local bookstores, since it appeared that if the local bookstores closed down, other retail businesses could take their place.

The planning agencies, of course, had taken into account the question of whether the proposed new centers would lead to "environmental impacts," including "urban decay," and concluded that it should approve the projects anyway. But the court states that the studies did not give reasons for those conclusions, and did not specifically address the combined impact of the two new shopping centers so close together. Further, of course, the studies did not address the impact of two Wal Mart supercenters because one of the reports didn't identify Wal Mart or even the existence of a second supercenter.

In the final analysis, the court really didn't even need the existence of the supercenters. It concluded that the EIR analysis was inadequate because the discussion of urban decay did not specifically address a number of issues raised by the opponents of the projects – relating both to business closures and the shut down of old Wal Mart facilities, which rarely are repopulated by other businesses.

> "The responses in the EIR's to these and other comments do not meaningfully address the issue of urban decay. [One of the EIR's] states that vacant buildings 'are part of the evolutionary change of the retail environment.' It then asserts that further analysis is outside th scope of CEQA because economic and social effects are not considered environmental effects under CEQA. . . . [The other report] is similarly incomplete. Ignoring the question of urban decay or deterioration, it simply replies that 'blight' is a legal term that does not apply. It also asserts that vacancy rates and business closures are purely economic impacts and therefore outside of CEQA. Finally, it states that a survey of vacant

> buildings ad been prepared and this survey demonstrated that 'retailers entering or leaving the market, relocations, re-leasing to new tenants or conversions to other uses is a normal part of a dynamic market."

The court gets increasingly critical of the EIR process as the opinion goes on. In response to the report's conclusion that the old Wal Mart space "can" be relet to other tenants, the court states that this is not a statement that the space "will" be relet.

In the end, although the court stated that "we do not quarrel" with the *Apple Valley* decision, indeed it is difficult to see how this court would have reached the same result, even had the case not involved a retail operator. The kinds of analysis used in this case could certainly have been mustered in opposition to a Wal Mart operation in *Apple Valley* had the fact of Wal Mart's identity been known. A great deal of the evidence analyzed here is extremely specific anecdotal accounts of Wal Mart's massive impact nationwide. It is virtually a reversal of Charley Brown's old statement about General Motors. Here, the opponents are pretty much saying that Wal Mart is too big and too powerful and "what's good for Wal Mart is bad for America."

The court then moved away from specific economic analysis and began talking about air and water quality impacts of the two major projects. In the end, in a few paragraphs, it bolstered its anti-Wal Mart decision with other broader conclusions supporting the decertification of the reports, so that it really is difficult to know what role the Wal Mart discussion had in that decertification at all, a tactic which certainly will influence the ability of the defendants to appeal, and will leave in the books the extensive discussion of why EIR's have to be economic planning documents.

Upon remand, the defendants pay all the legal costs (of course) and the reports are to be decertified, and the trial court must evaluate whether to enjoy all construction **and retail operations** at both centers pending the final preparation of the report.

Comment 1: For decades in California, environmental interests have played the "paper game" against targeted projects" with great success. With a cooperative court, and the vast array of available environmental commentators and experts, it is no great feat to muster a case that any given environmental analysis failed to adequately account for why this or that impact was not fully considered. Note that, once everything is in fact fully considered, the public agency most often would be permitted to go ahead with the project anyway, as it did here. But the environmental interests never have to reach the point of challenging the validity of the public decision – where they'd likely lose. Instead, they simply have to show that the process of decision was flawed because the report was flawed. It is not an adequate answer that the public agency wouldn't give a damn anyway. It has to jump through the hoops. Courts have been quite willing – given the proper cause – to continue to erect hoops, and, incidentally – to impose all the costs of the hoop building directly on the proponents. California has had a booming real estate economy for all this time, and apparently has been able to sustain the wealth redistribution resulting from this process. There is some question as to whether this can continue.

Comment 2: One can make an argument that the environmental "externalities" of land use decisions often are lost on public officials who are looking at positive economic and social benefits to their community presented by a new development project, and thus a rationale exists for requiring such officials to study hard a careful scientific analysis of these impacts before opting for the "quick buck."

But can the same policy analysis support the expansion of the EIR process into economic and social issues themselves? Here, one would assume that elected officials in fact are fully focused on these issues, both written and unwritten, proven and hypothetical, and have made the proper balance. Is there the same argument for empowering project opponents with the enormously powerful delaying tool that CEQA provides to those with more traditional environmental concerns?

One suspects that the California legislature ultimately will have to evaluate this question anew, and give the courts clearer instruction as to the proper scope of these reports, because it is clear that current courts are running a long way with the ball the legislature has handed to them.

Comment 3: Of course, it can always be argued that local officials are stupid blundering chamber of commerce types who respond only to economic and political power considerations and have far less judgment as to the economic and social issues presented by new development than that possessed by nonprofit "public interest" groups and their lawyers and financial supporters. If this is the case, however, is the remedy for such a state of affairs lie with the legislature or the courts. Or does it lie with the people? If elected officials make corrupt or stupid decisions – turn the rascals out!!

The fundamental question presented by cases of this type is whether economic or social policy will be made by the courts or the people. The answer is not always as easy as it sounds. Constitutional issues belong to the courts, of course, and environmentalists have managed to raise their agenda virtually to Constitutional status, at least in California. But how big can this bandwagon get? At some point, we must trust our future to our political process, for better or worse.

FEDERAL FORFEITURE; "INNOCENT OWNER" DEFENSE; TORRENS SYSTEM: Although, as to property held in ordinary, or "abstract" title, a mortgagee, upon the making of a mortgage loan, may become an "innocent owner" and may avoid federal forfeiture of the mortgagor's property due to mortgagor's criminal acts on the property, the same is not true of mortgagees of Torrens land. Such mortgagees must register their mortgages in the Torrens system before they have knowledge of the alleged criminal acts, or else they are subject to forfeiture under federal civil forfeiture laws. ***U.S. v. 392 Lexington Parkway South, St. Paul, Minnesota, Ramsey County, 2005 Westlaw 2179155 (9/7/05)***

Gore acquired certain property in 2002 and borrowed money about the same time from Long Beach, giving Long Beach a mortgage on the property. The property consisted of some land that was subject to the Minnesota registered title system, known as Torrens, and some land that had not been subjected to that system, which the court described as "abstract" land.

Long Beach failed to record or register its mortgage at the time it took the mortgage. A year later, Gore, already indicted for cocaine trafficking, took out a second loan secured by the property and gave a mortgage to MG III. MG III had no actual knowledge of the indictment or the drug activity. Astonishingly, MGIII also failed to record or register its mortgage promptly .

Six weeks after the MG III loan, the U.S. Government filed a *lis pendens* on the property stating that the Government had undertaken an action to forfeit Gore's interest in it. A month after that, MG III filed its mortgage for recordation and for registration on the Torrens portion. Long Beach didn't get around to recording until Gore defaulted in and it sought foreclosure several months after the MG III filing.

The mortgagees noted that the federal statute defines "innocent owners" as including mortgagees and says that "an innocent owner's **interest in property** shall not be forfeited." They argued that when they took their mortgages they obtained an interest in the property within the meaning of the federal law, and that the only relevant question was whether they had knowledge of the mortgagee's criminal problems at that time.

In fact, the court concluded that both mortgagees had not actual or constructive notice of the criminal issues at the time that they took their mortgages. But it concluded that the question of whether those mortgages represented an "interest in the property" depended upon state law. It conceded that as to the property that was "abstract" land, a mortgage interest in the land becomes valid upon conveyance of a mortgage in Minnesota. But, under Minnesota's Torrens system, the court concluded, there is no interest in property unless and until a mortgagee actually registers the mortgage with government authorities.

At the time that the mortgagees registered their mortgages, a *lis pendens* had been filed, the Government had filed its *lis pendens* and the mortgagees could not be "innocent purchasers" under the federal law because they had constructive notice of the forfeiture claim.

Comment 1: It does seem bizarre that the same mortgagee is protected as to some land and not as to others as a consequence of the dual recording system in Minnesota. Clearly this was not the intent of the drafters of the system, but it must be conceded that the focus on the registration requirement as a condition of validity of one's interest is a vital element of registration systems.

Comment 2: We're all comfortable in the U.S. with our own system, but required registration has a lot to recommend it, especially in a more sophisticated and organized society, when it really isn't unreasonable to expect people to carry out transactional formalities.

There are other problems with Torrens, however. First, it's expensive for the government. (But perhaps less so as computer technology develops.) Second, all the existing properties would have to go through a registration process, and this requirement has killed the proposal for registration in most places it has been raised.

FEDERAL LANDS; MINING CLAIMS; TREATY OF GUADALUPE HIDALGO: Occupiers of land owned by the United States by virtue of the Treaty of Guadalupe Hidalgo and presidential decree had no claim to land without a "legal entry," "lawful filing of record," or "valid settlement by law." ***United States v. Fennell, 2005 U.S. Dist. Lexis 16651 (D.N.M. June 7, 2005).***

The United States sued occupiers of federal land for *inter alia*, common law trespass. Occupiers responded by claiming title to the land based on unpatented mining claims, arguing that their residency was incident to their gold mining activities. The occupiers claimed an interest in the land by virtue of Mexican mining operations that predated the Treaty of Guadalupe Hidalgo; however, they were unable to establish the exact location of an alleged Mexican settlement. The court found the land at issue became National Forest Land in 1907 by a Presidential Proclamation issued by Theodore Roosevelt. Because the occupiers could provide no evidence of legal entry in the form of an application for purchase or patent, no lawful filing of record for a town in the form of a patent or plat, and no valid selection in the public record, the occupiers were trespassers on National Forest Land. Further, even if the occupiers owned unpatented mining claims dating before 1872, the United States maintains fee title to any unpatented claims by virtue of the Surface Resources Act of 1955.

ROAD CONSTRUCTION, PUBLIC LANDS, EASEMENTS: Counties must alert administrative agencies before undertaking anything but routine maintenance of roads on public land. ***Southern Utah Wilderness Alliance v. Bureau of Land Management, 2005 WL 2160126 (10th Cir.(Utah)).***

The case presents some extensive background that must be summarized. Before 1976, a statute known as R.S. 2477 had been in place for more than 100 years. R.S. 2477 encouraged local governments to build roads on public land, with a grant by the federal government of "the right of way for construction of highways over public lands, not reserved for public uses." In 1976, Congress froze this right. Essentially, the new law granted no new rights of way, but allowed local governments to maintain rights of way in existence in 1976. Interpreting the rights created under R.S. 2477 has proved problematic, because the law did not provide guidance about the meaning of "right of way," and local governments, over the course of the statute's life, often failed to formally document the rights of way supposedly established pursuant to the statute.

This case arose when three counties in Utah sent workers onto Bureau of Land Management land to grade sixteen roads. None of the roads had been graded previously, but some of them showed signs of previous construction or maintenance activity. Arguing that the roads were actually unimproved trails not amounting to rights of way under R.S. 2477, a nature conservancy group sued the BLM to stop the grading, and the BLM in turn sued the counties. The counties claimed the roads were valid R.S. 2477 rights of way. In the trial court, the court decided the BLM should determine whether the roads were rights of way under the statute, or something less. After a BLM investigation, the BLM decided that the counties lacked valid rights of way for 15 of the 16 "roads." The trial court then affirmed the BLM's decision in its entirety.

The appellate court, after some lengthy procedural analysis dealing with whether the trial court should have reviewed the BLM's decision *de novo*, remanded the case for the court to determine whether the roads were in fact rights of way established under R.S. 2477, and the appellate court provided substantial guidance regarding the standards the trial court should use in its determination.

Perhaps the most important point of the decision lies in the directive that counties proposing to work on roads over federal lands should check with the agency in charge (the BLM or National Forest Service) before performing any work beyond routine maintenance. Undocumented roads and trails crisscross the nation, particularly in the West. Whether the public has access to those paths is proving a very contentious issue, claimed by both sides in fights over public and private property rights, and preservation versus development.

GUARANTY; IDENTITY OF GUARANTOR: A personal guaranty on an open account for construction materials failed to sufficiently identify the principal debtor by name where there was no entity identified as

"Applicant" in the credit application, and therefore was unenforceable, despite clear intent of the parties. ***McDonald v. Ferguson Enterprises, Inc., 2005 WL 1531070 (Ga.App., June 29, 2005).***

Plaintiff claimed Defendant was liable pursuant to a personal guaranty agreement for "all sums owed by his company" on an open account for construction materials. While the "Terms Section" of the credit application immediately above the personal guaranty section identified the applicant for credit as the "undersigned applicant", the two undersigned signatories were specifically identified as "Witness" and "Owner/Officer". No one was identified as "Applicant". On that basis, the Court of Appeals of Georgia applied the Statute of Frauds and barred enforcement of the guaranty, despite the obvious intent of the parties.

INSURANCE; DEFINITIONS; "PERSON:" In insurance policy providing coverage for wrongful eviction, a "person" wrongfully evicted must be a human being, and not a business. ***Mirpad v. California Insurance Guarantee Assoc., 34 Cal. Rptr. 3d 136 (Cal. App. 9/19/05)***

Mirpad was the owner of commercial property, and paid for a liability policy related to that ownership issued by a predecessor of CIGA.

Mirpad's managing agent evicted an existing tenant on the premises and the tenant and one of its principles sued Mirpad for wrongful termination and eviction. Mirpad tendered defense of the lawsuit to its insurer, which denied coverage. Mirpad then defended the suit at a cost of in excess of $500,000 and sued the successor insurer for damages.

There was no question in the case that if the policy covered the alleged injury, there was a duty to defend. The case law clearly established such a duty except where the existence of a duty depends upon an issue of law. The question here, of course, was a legal one – whether the policy covers the claim at all.

The liability policy contained a provision for "personal Injury and Advertising Injury Liability." Pursuant to that coverage, the insurer promised to "pay those sums to which this insurance applies, that the insured becomes legally obligated to pay as damages because of personal injury." "Personal injury" was defined elsewhere in the policy to include ". . . injury other than bodily injury arising out of one or more of the following offenses: (1) false arrest, detention or imprisonment; (1) malicious prosecution; (3) wrongful eviction from, wrongful entry into, or invasion of the right of private occupancy of: (a) a room; (b) a dwelling; or (c) premises; that a person occupies by or on behalf of its owner, landlord or lessor. . . "

The insurer took the position that coverage under the above language was available only when the alleged wrongful eviction was of a human being, and not a business entity. As the alleged wrongful eviction in this case was of a corporate entity, the insurer maintained, there was no coverage as a matter of law, and therefore no duty to defend.

The trial court, relying on the Webster's Dictionary definition of "person," disagreed, and found coverage based upon the notion that the word "person" as used in the policy included either a natural person or a corporate entity. The court of appeals here reversed, finding that the term "person," in the policy, as a matter of law, meant only a natural person, and not a business entity..

The court stated that it "must read the quoted term ["person"] not in isolation, but in the context of the entire policy." At another point it stated that its approach was consistent with the "principle that a court, in determining the plain meaning of a policy language must not only interpret that language in its 'ordinary and popular sense,' but also in the context of its usage in the policy itself." It noted that the policy consistently used the term to refer only to natural persons, while corporate and other business entities were referred to as "organizations." It commented that if it were to view "person" as to include "organizations," then the policy's use twenty times of the phrase "person or organization" would be superfluous and the single reference to "organization" in twelve other places might be ambiguous.

The court further noted that the "wrongful eviction" language in the policy referred to places where people live. The policy used the terms "room," "dwelling," or "premises." It stated that the word "premises" "is the more general of thee three terms, but, as noted, settled rules of construction compel us to conclude that it is of the same class as the other two."

Comment 1: The case is most likely correct, although one certainly can quibble with elements of the analysis. Is it really true, for instance, that an "organization" cannot occupy a "room?" Does the term "room" exclusively connote a dwelling place? If it does not, then the phrase "room, dwelling or premises" may have a different meaning than suggested. Perhaps the use of the three terms was to identify that a single room in a multi-tenant building could be the subject of a wrongful eviction action, as could either a dwelling or some other premises other than a dwelling. But the frequent use throughout the policy of "person or organization" also was convincing to the editor as it was to the court. When the drafters of the policy provided coverage for the wrongful eviction of a person they probably had in mind a natural person, not a business entity.

Comment 2: Of course, the ordinary rules of construction don't govern insurance policies – the classic contracts of adhesion. What the drafters intended in their back room at the home office is not necessarily controlling. Nevertheless, these policy language must have some standard meaning. This case just means that clients have to pay their lawyers to read policy language carefully to be sure they're getting the coverage they expect. For lawyers, then, "it's a good thing."

INTERSTATE LAND SALES FULL DISCLOSURE ACT; FORUM SELECTION CLAUSE: A mandatory forum selection clause requiring all litigation to take place in Korea does not violate public policy underlying the Interstate Land Sales Full Disclosure Act. ***Choi v. Samsung Heavy Industries Company, Ltd., 129 Fed. Appx. 394 (9th Cir. 2005).***

Purchasers of condominium units located in Korea brought fraud-based claims against the builder of the units. The Federal District Court dismissed the fraud claims. On appeal, the purchasers contended that a mandatory forum selection clause that allowed venue only in Korea violated the Interstate Land Sales Full Disclosure Act. The Ninth Circuit disagreed, saying the clause did not violate "strong public policy" in the Interstate Land Sales Full Disclosure Act. Further, the court, citing *Richards v. Lloyd's of London*, 135 F.3d 1289 (9th Cir. 1998) held that anti-waiver provisions within the Act do not invalidate forum selection clauses. The court based its holding on precedent addressing anti-waiver provisions within the Securities Act of 1933 (the model for the Interstate Land Sales Full Disclosure Act).

INTERSTATE LAND SALES FULL DISCLOSURE ACT, LIABILITY, SECONDARY DEVELOPER: Where developer who sold lots to landowners later sold subdivision and development responsibilities to secondary developer who did not participate in the sales to plaintiffs, the court will not hold the secondary developer liable under the Act, absent some clear managerial connection between the developers. ***Paniaguas v. Aldon Companies Inc., 2005 WL 1983859 (N.D.Ind.).***

Plaintiffs, purchasers of lots in a subdivision, sued the former developer and the current developer of a subdivision under the Interstate Land Sales Full Disclosure Act for, *inter alia*, failing to pave streets, light streets, and strictly enforce building covenants. Originally, the purchasers bought their lots from Developer A, Developer A sold the remainder of the undeveloped subdivision lots to Developer E. As part of the purchase agreement, Developer E assumed the responsibility for paving streets, street lighting, enforcement of restrictive covenants, and control over the architecture committee. Plaintiff purchasers sued both developers for the alleged failures. Upon a motion to dismiss brought by Developer A and Developer E, the court dismissed Plaintiffs' claim only in regard to Developer E. The court held that because Developer E was neither a developer under the Act's definition nor an agent of a developer under the Act's definition, Developer E could not be held liable. The court interpreted the Act's definition of a developer (any person who, directly or indirectly, sells or leases, or offers to sell or lease, or advertises for sale or lease any lots in a subdivision) to be limited to defendants who are involved in the sales process. Because there was no transaction between the plaintiffs and Developer E, the court found E could not be liable under the Act. However, the court refused to dismiss the claim against Developer A.

LANDLORD/TENANT; ASSIGNMENT AND SUBLET; LANDLORD'S CONSENT: Landlord is not in breach of a lease for unreasonable failure to consent to a sublease where the tenant has not produced a ready, willing, and able subtenant; and attorney's fees in such an action do not have to be assessed using the lodestar method. ***WHTR Real Estate Limited Partnership v. Venture Distributing, Inc., 825 N.E.2d 105 (Mass. App. Ct. 2005).***

Lessee wished to relocate and determined to sublease the property. Lessee's broker contacted USCO with an 'as-is' offer of sublease, and USCO responded with a counteroffer containing additional conditions. Lessee did not respond directly to the conditions contained in the counteroffer, but instead prepared a sublease and forwarded it to USCO's in-house counsel, who took no further action.

Lessee also forwarded the proposed sublease to Landlord with a request for consent. Landlord requested financial information from USCO's CEO, who did not respond. At the same time, USCO was negotiating for a different space with another party. USCO did conduct a walk through of Lessee's space, and prepared a list of seventeen items needing "repair/testing prior to signing a lease." Two weeks later, USCO signed a lease for the other space.

Landlord filed suit against Lessee for breach of the lease, requesting rent, attorney's fees, and costs. Lessee counterclaimed alleging Landlord had breached the lease by poisoning negotiations between Lessee and USCO and by unreasonably withholding consent to the proposed sublease. The Superior Court found Lessee in breach and awarded rent, attorney's fees, and costs to Landlord. Lessee appealed the ruling on the breach, and Landlord appealed the amount of costs and attorney's fees awarded.

The trial judge found that throughout the process, Lessee's responses to Landlord's requests for information and documents were slow, if they occurred at all. Lessee also never fully addressed USCO's counterproposal or the separate list of issues with the property. A signed sublease was never presented to Landlord for approval.

The Appeals Court held that the trial court had properly found that breach for failure to consent ought not to be found where the tenant has not produced a ready, willing, and able candidate to take on the tenant's full obligations under the lease. The court also noted that claims regarding interference with negotiations were too speculative given the uncertain state of the negotiations and a lack of evidence that USCO was ever ready to merely step into Lessee's place under the lease.

Likewise, Landlord's appeal for larger attorney's fees was dismissed based on a finding that the trial court had not abused its discretion in finding Landlord's submitted amounts unreasonable. The court held that even uncontroverted submissions must be found reasonable, and the trial court was not required to use the lodestar approach (hours reasonably spent multiplied by a reasonable hourly rate) to test reasonableness. The Appeals Court clarified that *Fontaine v. Ebtec Corp.*, 613 N.E.2d 881 (Mass. 1993) does not require use of the lodestar method, but merely notes that such an approach can prove to be advantageous. The Appeals court found that Superior Court had considered appropriate factors and had not abused its discretion or committed clear error.

Comment 1: This case is troublesome if it means what it says, but it probably doesn't. First, the court said that it was upholding the trial court's ruling that a completed sublease must be presented to the landlord in order for the landlord to be liable for unreasonably refusing consent:

> "Among [the judge's rulings] was the a ruling that a landlord is not in default for failure to consent unless the tenant produces a candidate ready, willing and able to fulfill the tenant's obligations under the sublease. The tenant has not persuaded us that the judge ruled in error." [Citing Friedman on Leases for this verbatim rule.]

The tenant maintained that this ruling is too narrow, as it does not take into account the circumstance where the landlord indicates its refusal to consent or unreasonably makes demands of the proposed subtenant so as to block further negotiations. The court's response to this argument indicates that it might entertain such a position in the appropriate case, but that this case did not support such an analysis:

> "We need not determine whether the judge's ruling was too narrow. Any benefit to the tenant from an expanded rule is obviated by the judge's conclusions, amply supported by her findings, that 'there is no evidence that the parties were even close to resolving the terms of the sublease. . . There were too many uncertainties and unresolved issues to legally bind either USCO or [the tenant]. . . ."

This sounds like a broader test, but the balance of the trial judge's quoted ruling reiterates the requirement for a completed lease.

Comment 2: The Friedman excerpt the court relied upon now appears in Section 7:3.4[D]3 in the Randolph edition. It is based upon a 1991 Illinois case, *Golf Mgmnt. Co. v. Evening Tides Waterbeds, Inc.,* 572 N.E. 2d 1000, which indeed makes the statement, and cites other Illinois authority for the point.

Comment 3: On first blush, the editor agreed with the tenant's basic position (but still agreed with the court's failure to apply it here.) But, upon sleeping on the issue, the editor concludes that there likely is no case in which a tenant, without having made contractual arrangements in advance, should expect a landlord to indicate approval to a subtenant prior to the tenant's reaching agreement with that subtenant. The landlord is entitled to know the terms of the sublease. If the landlord wanted to be cooperative, of course, it could "vet" the proposed subtenant's credit and respond to various questions concerning it's views on various elements of the sublease prior to the completion of negotiations with the subtenant. This would certainly make subleasing easier. But that is not the landlord's job. If the tenant desires that the landlord be required to make an advance approval of a proposed subtenant, it should bargain for that (the landlord should still get a "second bite" based upon any changed circumstances when the sublease is completed).

This is not to say that the landlord has the right at any time to be obstructionist – to make unreasonable threats or to take unacceptable and unreasonable positions. If the landlord should do that, even before the proposed sublease is completed, the landlord would be in breach of any duty the landlord had to be reasonable. But silence in this case is not unreasonable.

Comment 4: It is worth noting that there is neither a "majority rule" nor a "developing trend" supporting an implied duty of reasonableness in this area. There are some cases – some overruled by statute. But there is an equal number of modern cases that have rejected the proposition after being confronted with the rulings of their sister states. Friedman details all the cases Mr. Friedman was a fan of the implied duty of reasonableness in this area. The current editor of Friedman (your DIRT editor) isn't. Hey – it's hardball. If you want to have judicial review of the reasonableness of a landlord's decision in this area, put it in the lease.

LANDLORD/TENANT; ASSIGNMENT AND SUBLET; LANDLORD'S CONSENT: Landlord is unreasonable in withholding consent to assignee based upon the fact that assignee will compete with landlord's business, especially when landlord has acquired the leased premises following the lease to tenant by another landlord. ***Tenet v. Jefferson Parish Medical Center, 2005 U.S. App. LEXIS 20283 (5th Cir. 9/21/05)***

Tenant entered into a lease in a shopping center for an outpatient surgical center. The lease provided that Tenant could use the property for "out patient surgical procedures and general medical and physicians offices, including related uses and for other purposes reasonably acceptable to Landlord." The lease provided that Tenant had to obtain Landlord's consent to any assignment or sublet, but that consent would not be unreasonably upheld.

Later, the landlord transferred the shopping center fo Jefferson, which operated a hospital in the area and acquired the space for "strategic purposes" for future expansion.

Tenant then sought to sublease the space to Pelican, which operated an occupational medical clinic – which provided a range of medical services to employees of identified corporate clients, rather than to the general public. Jefferson objected on the grounds that Pelican's proposed business was not within the permitted activities under the lease and that Pelican would compete with activities that Jefferson was conducting on nearby premises.

Tenant brought suit based on the allegation that Jefferson's refusal to consent to the sublet was unreasonable. The federal district court granted summary judgment to Jefferson, ruling that whether Jefferson was reasonable ought to be determined with reference to Jefferson's individual situation.
On appeal: *Held, Reversed.*

The Court of Appeals had no problem finding that the occupational medial clinic fit within the description of "medical and physician's offices." Interestingly, it cited a case in which an orthodontist's office was held not to be within the description of "general dentistry." But that case, based upon specialized dentistry terms, had no impact here.

As to whether Jefferson was reasonable in refusing to consent to a competitor, the court made two alternative findings.

First, the court held that a landlord is unreasonable when it refuses to consent to a sublet to a party that will compete with business that the landlord is conducting nearby. It cited a thoughtful New Mexico decision that acknowledged that a landlord can take it's own economic interest into account, but that this interest must relate to the premises in question (apparently expanded to include the shopping center of which the premises are a part) and the landlord cannot withhold consent to improve its "general economic interest." Although the opinion could be more clear, the court apparently was of the view that the withholding of consent was done to decrease competition to the hospital's business located outside the shopping center of which the lease was a part.

Second, the court held that, in any event, the perspective from which the landlord's decision will be judged is an objective one based upon the nature of the landlord **at the time of the letting.** Thus, tenant is enabled to make judgments as to what is or is not likely to be viewed as reasonable taking that landlord into account, rather than being subject to differing standards as the reversion changes hands. Under this standard, of course, the Jefferson's position would have been unreasonable whether or not it was protecting its medical business within or outside the center, since the original landlord had not been in the medical services business.

Comment 1: Based upon what the court says its research revealed and upon the available discussion in Friedman on Leases (Randolph Edition), at Section 7:3.4, this is perhaps a "perfect storm" consent issue of virtually first impression. Friedman cites very few cases on the subject of whether a landlord can withhold consent for anticompetitive purposes, and only two cases involving shifting landlords. Thus this case is a very significant precedent.

Comment 2: On the question of withholding consent for anticompetitive purposes, Friedman does cite one California case, discussing the issue in *dicta,* and another case upholding a shopping center landlord's refusal to consent to an assignment that would lead to competition with other landlord's other businesses conducted within the shopping center where the proposed assignment would occur. Further, in *Medinvest Co. v. Methodist Hosp.,* 359 N.W. 2d 714 (Minn. App. 1984), a hospital landlord was permitted to withhold consent to an assignee who would compete with landlord in an adjacent and "skyway connected" building. The court emphasized that the landlord's primary business venture in both buildings was the provision of medical services, rather than earning rentals from leasing space.

Edelman v. F.W. Woolworth Co., 252 Ill. App. 142; 1929 Ill. App. LEXIS 665 (Ill. App. 1929) is a seminal case, cited by Friedman and all of the above courts, including the instant court, for the proposition that the landlord ordinarily is unreasonable in trying to protect itself from competition at other locations through its decision to deny consent to an assignment or sublease.

Comment 3: Perhaps the more intriguing question before the court was whether the tenant could rely on the identity of the landlord at the time of letting, so that the landlord's reasonableness in determining whether to consent should be judged by objective standards assuming a landlord with business interests similar to that original landlord. Friedman cites only one clear case on this point, a 1969 New York decision in which a religious institution acquired a building subject to an existing lease and later refused to consent to the assignment of the lease to family planning clinic on the grounds that the activity was inconsistent with its principles. This decision was held to be unreasonable, as the original landlord had no objective basis to object on those grounds.

Comment 4: The editor is of the view that all the bells haven't rung on the issue of shifting landlords. Maybe we can "carve out" the religious institutions and hospitals, but in fact, in any long term lease, a tenant ought to expect that the landlord's future business interests will evolve, and if a new landlord is within a foreseeable range of development that the old landlord might have experienced as well, then the tenant should not be able to claim that the new landlord's actions are unreasonable just because the old landlord, as that landlord existed at the time of letting, might not have had a basis to object. This cannot be what the parties reasonable expected, and analysis of reasonable expectations should be the primary tool in resolving these issues.

LANDLORD/TENANT; DEFAULT: Under the literal reading of a default clause in lease, a "nonmaterial but non insignificant" breach tenant breach consisting of demolition of a storage shed and construction of a larger unit in its place might otherwise justify termination by the landlord, but equitable concerns would prevent termination on the current facts. ***DiBella v. Fiumara, 828 N.E.2d 534 (Mass. App. Ct. 2005).***

The parties entered into a contractual arrangement for the purchase of an existing adult entertainment business, the Golden Banana Club, and a lease of the property the club occupied. The Lease contained two provisions of note here: one barring structural alterations without Landlord's consent (not to be unreasonably withheld), and the other providing for Tenant's default upon failure to observe the terms of the Lease.

Tenant desired improved storage for the business, and determined to demolish and rebuild a dilapidated shed that abutted a corner of the business. The new storage area was larger and sturdier, consisting of an 18'x 39'x 20' structure with a basement, and was constructed at a cost to Tenant of $132,000. While the new storage was being constructed, Landlord drove by the site, took photos, and interviewed the contractor. Landlord made several visits to the site, and at one point told the contractor it "looked good."

Approximately one week after first discovering the work, Landlord sent Tenant a default notice for failing to obtain written consent. Tenant responded that the improvement would benefit the property and Landlord and that withholding consent would be unreasonable. Landlord then sent a denial of consent citing concern regarding damage to a load-bearing wall, exposure to additional property taxes, and the possibility of resulting zoning issues.

Tenant continued construction for an additional month, then stopped in midconstruction. Shortly thereafter, Landlord brought suit for default on the Lease. The trial court found that Tenant's failure to obtain prior written consent constituted a breach of the Lease, but that the breach was not material and therefore did not justify termination of the lease.

The Appellate Division of the District Court then reversed the materiality ruling, finding that Tenant was on notice of possible termination under the provisions of the Lease, that Tenant had willfully breached those provisions, and that no action of Tenant could undo the harm done to Landlord.

Tenant appealed, arguing for reinstatement of the trial court's decision, and Landlord appealed on the ground that the default clause in the Lease should be dispositive as a matter of law regarding materiality. The Appeals Court first noted that a materiality standard would apply in the absence of a default clause, and that the clause must therefore reach at least some non-material breaches. The court also noted that even where operating under a default clause, insignificant or accidental breaches will not justify termination, concluding therefore that a default clause can reach non-material but significant breaches.

Notwithstanding this conclusion that the breach need not be "material," the court noted that equitable concerns will override contractual requirements for forfeiture or termination of a lease,

Relying on a line of Massachusetts cases and upon Restatement (Second) of Property (Landlord & Tenant) § 13.1,. The Appeals Court found that the trial judge had properly made factual determinations regarding the lack of negotiation effort towards the default clause and also with respect to materiality under the detailed standards presented in Restatement (Second) of Contracts § 241 (1981). Accordingly, the Appeals Court found that the Appellate Division failed to accord proper deference to the Trial Court's findings, and could not be allowed to overrule factual findings which were properly reached.

The court therefore reversed the Appellate Division's ruling with respect to materiality of the breach, but upheld the ruling with respect to its finding that the pure language of the default clause demonstrated that the breach was not "insignificant and would support forfeiture of the lease in the absence of other equitable considerations. Landlord was given thirty days to petition for a hearing into whether such equitable considerations existed, although the court also noted that Landlord had acknowledged in its brief that the trial court implicitly found such considerations to exist, rendering such a request likely futile.

Comment 1: Here the court concludes that when there is a clause in the lease that specifically identifies certain conduct as a breach, the question of whether a breach is material or not really doesn't matter – the fact that the default exists should establish conclusively that the parties treated this conduct as significant.

This distinction between "nonmaterial" breaches and "not insignificant" breaches is one that the editor hasn't seen before. The editor first reaction to it is favorable, as the editor has long supported the notion that there is a distinction, often blurred by the courts, between "contract right" and "equitable remedy." Whether a party should have equitable enforcement of its rights ought to be measured by the court in the individual instance. Sometimes a party will be left to its other contract damages.

But the editor has not yet concluded that such equitable limitations ought to limit the options of a landlord to forfeit a lease where the tenant has clearly breached. An eviction is not an injunction – it simply is a recognition of wrongful possession and restoration of possession to the lawful owner. This is a very basic right, and where the parties have contracted for conditions under which this right exists, courts should uphold it.

Comment 2: There is still some question as to whether the frequent visits by the landlord, during which the landlord said nothing but good things about the project, ought to lead to another form of equitable intervention – estoppel based upon laches. The estoppel concept modernly may be used to bar both equitable and legal remedies in most common law courts. Estoppel is based upon more than the "equitable sifting of the facts," and depends, in most cases, upon some inequitable conduct on the side of the party seeking the remedy to be barred. The editor views estoppel as a necessary lubricant to the joints of the law, and if that is all the court means here by "equitable enforcement," the editor agrees completely. But editor thinks the court's view of the equitable discretion of the court is broader – similar to that which would apply when the court decides whether to grant an equitable remedy like an injunction. Such discretion is too broad where, as here, there is a clear, deliberate, and uncurable breach of a specific contractual provision.

LANDLORD/TENANT; FIXTURES; TENANT'S REMOVAL RIGHTS; Lease provision stating that all "buildings, structures and improvements" will remain with the landlord but also stating that tenant may remove trade fixtures is not ambiguous, and as a matter of law tenant may remove items that legally constitute trade fixtures, including a canopy over gas pumps at a convenience store. ***Lay Bros., Inc. v. Golden Pantry Food Stores, Inc., 273 Ga.App. 870, 616 S.E.2d 160 (2005).***

The landlord pointed out that the lease contemplated that the tenant could demolish all the buildings on the premises and build a new convenience store, which Tenant did. The landlord argued that to permit the tenant to remove trade fixtures could be read to permit the tenant to remove the buildings themselves, which would be inconsistent with the apparent intent of the parties to leave the replacement buildings for landlord's use.

The court dodged the issue simply by saying that the tenant didn't argue that it could take the buildings, only the canopy.

(Note: There was question about the validity of the assignment to Landlord, but that had no impact on the outcome in this aspect of the case.)

Comment: The editor doesn't wish to dodge the issue. A common exception to the concept that almost anything the tenant puts on the premises is a trade fixture arises when the tenant removes or destroys existing elements of the premises and replaces them with its own. In such a case, it is far less likely that a court will permit the tenant to remove such improvements unless the lease unambiguously so provides.

Despite what the court says about the canopy, the language quote above would not unambiguously give the tenant a license to remove buildings that it constructed to replace other buildings on the premises that it had demolished.

LANDLORD/TENANT; INSURANCE; SUBROGATION; TENANT AS IMPLIED CO- INSURED: Maryland rejects concept that tenant is implied co-insured and automatically immune from subrogation claim by landlord's insurer where tenant negligence causes loss to premises – subrogation may be barred where tenant legitimately expects that landlord will rely solely on insurance, but analysis is case by case. ***Rausch v. Allstate Insurance Co., 882 A.2d 801 (Md. 2005)***

There were two cases here – both residential tenancies. The leases did not contain waiver of subrogation clauses commonly found in commercial leases. In both cases, the court assumed that the tenant had negligently caused significant fire damage to the landlord's premises. The court addressed a rule that some have characterized as a majority rule that tenants are immune from subrogation suits from the landlord's insurer, even where there is no waiver of subrogation clause, because the cost of insurance is a component of the total rent, and thus the tenant pays rent upon which the landlord relies in buying insurance. Therefore, the tenant is an "implied co-insured."

In one of the cases here, there was some evidence in the lease that the landlord and tenant had agreed contractually that the tenant would be liable to the landlord, at least, if the tenant negligently damaged the premises. There was a "yield up" clause that required that the premises be returned in the same condition as received, except for ordinary wear and tear. There was a clause requiring the tenant the acquire and maintain insurance to cover any losses to the tenant due to fire in the premises and requiring the tenant to obtain "adequate liability insurance." There was language cancelling the lease if the premises were rendered uninhabitable by fire. And, perhaps most significant, there was a clause stating that tenant was responsible "for any and all damages to the Property caused by any act of negligence of Tenant," and making the tenant responsible for all repairs, replacements and related services of tenant negligently damages the Premises.

There was also, however, a clause indicating that tenant would comply with the fire safety requirements of any insurance policy maintained by landlord, suggesting of course that the parties anticipated that the landlord would have such insurance.

In the second case, the lease again provided that the tenant would be liable to the landlord for the results of tenant negligence. It said nothing about the landlord procuring insurance. In fact, in both cases, the landlord did have an insurance policy which paid a substantial portion of the damages in question (caused by tenant negligence) and the insurance companies were seeking to make subrogated claims.

The court said that the law was reasonably clear that it was possible for the landlord's insurer to have the right to make a subrogated claim against tenant. Subrogation law reached that far. It also acknowledged that there had to be a claim available to the landlord against the tenant in order for subrogation to arise. But in this case that requirement seemed to exist. .

The court further stated that the question was not whether the tenant was liable to the landlord for negligent injury to the premises, but whether the tenant would be liable to the insurer. It noted that there might in many cases be a question as to whether the parties reasonably anticipated that the landlord would rely upon the landlord's insurance as compensation for any such damage. Of course, as stated, in many circumstances, commercial leases expressly provide for waiver of subrogation. But the court noted that, even in the absence of an express waiver of subrogation in the lease, many courts had been persuaded that the economic reality of the situation compelled the conclusion that the that the tenant's rent was paying the cost of the landlord's insurance. As a consequence, these courts have concluded that the landlord and tenant implicitly intended that the tenant be a "co- insured," even when the lease specifically imposed liability on tenant to landlord for specified acts of negligence. There can be no claim by an insurer against such a "co-insured" party.

But the court, after considerable analysis, including citing many of the relevant cases, concluded that the "implied co-insured" rule should not be the rule in Maryland. Rather, the court would look on a case by cases basis to ascertain what the parties had in mind with respect to tenant-caused injury. It commented: "courts have no business adding insured to an insurance policy in order to achieve their perception of good public policy."

In the end, although the court concluded that Maryland would not follow the "implied additional insured" theory and that it would look at these matters on a case by case basis, it included two important *caveats* that will enable effective planning in many circumstances – cases in which, notwithstanding the failure of the lease to waive subrogation claims, a court nevertheless should not permit subrogation, even though the tenant is negligent and might be liable to the landlord for uninsured claims:

> [1] "If, under the lease or by some other commitment, the landlord has communicated to the tenant an express or implied agreement to maintain fire insurance on the leased premises, absent some compelling provision to the contrary, the court may properly conclude that, notwithstanding a general "surrender in good condition" or "liability for negligence" clause in the lease, their reasonable expectation was that the landlord would look only to the policy, and not to the tenant, for compensation for fire loss covered by the policy. That expectation would constitute an implied commitment in the lease to relieve the tenant of liability to the extent of the policy coverage and it, too, would therefore preclude a subrogation claim."

> [2] "If the leased premises is a unit within a multi-unit structure, absent a clear, enforceable provision to the contrary, a court may properly conclude that the parties anticipated and reasonably expected that the landlord would have in place adequate fire insurance covering the entire building and, with respect to damage caused by the tenant's negligence to parts of the building beyond the leased premises, would look only to the policy, to the extent of its coverage, for compensation. That expectation has a rational and practical basis. Whatever general common law liability a tenant may have for damage to another person's property caused by the tenant's negligence, it is not likely, unless faced with a very clear contractual obligation to the contrary, that the tenant is thinking beyond the leased premises or, as a practical matter, would be able to afford, or possibly even obtain, sufficient liability insurance to protect against such an extended loss. Nor should the law encourage the economic waste that would result from multiple layers of insurance by the individual tenants to cover the same loss."

The court remanded both cases before it for n individual determination as to whether subrogation is appropriate.

Comment 1: The case, which relies heavily on Friedman on Leases (albeit the 4th (non-Randolph) edition – harrumph) also cites and discusses most of the leading cases on both sides of the question, and is an excellent resource for information on how this split is developing around the country.

Some cases find that the tenant is a complete co-insured, and others find simply that subrogation claims cannot be brought. Many, as the court notes, do not involve liability claims as clear as those involved in the present case.

Comment 2: The problem with "case by case" determinations, of course, is that there is no predictability. Parties can't allocate risks by bargaining nor adequately predict and efficiently protect themselves against risks that do exist. But is this a case where predictability would make much difference? Remember we're already excluding cases in which the parties have bargained for a waiver of subrogation. If they didn't enter into a waiver, then are they really in need of a predictable rule as to whether subrogation will be available anyway?

Comment 3: Waivers of subrogation are virtually "freebies." Most insurers don't object to them (the risk is the same anyway in commercial leases, at least) and thus all lawyers on both sides should seek to obtain such mutual waivers. The cases where there won't be waivers are cases like these, where it is unlikely that the tenants had the sophistication or bargaining power to have much to say about the terms of the lease, and the landlord consequently has no incentive to confer subrogation protection against the tenant even though, in many cases, again, it would do the landlord little harm.

LANDLORD/TENANT; LANDLORD'S LIABILITY : A landlord may not hold its tenant liable for the landlord's own negligence. ***Danielson v. Jameco Operating Corp.*, 800 N.Y.S.2d 421 (A.D. 2 Dept. 2005).** The plaintiff fell on ice in an alleyway owned by the defendant and leased to third party, Adonia Pizza Corp. In a third-party suit, the defendant landlord attempted to hold its tenant liable for damages resulting from the fall. The court held, however, that the landlord failed to demonstrate that it was an out-of-possession landlord that lacked control over the area. Furthermore, the court stated that the lease does not reflect a clear intent for the tenant to indemnify the landlord for the landlord's own negligence or to procure insurance for their mutual benefit.

LANDLORD/TENANT; LANDLORD'S LIABILITY; LIABILITY FOR THIRD PARTY CRIMINAL ATTACKS: . Landlord not responsible for failing to provide sufficient security against assault on the premises when landlord is not in control of the premises, even when it has the power to exercise control. ***Krause v. Spartan Stores, Inc., 816 N.E.2d 696 (Ohio App. 6 Dist. 2004***)

Appellant Krause appeals a lower court summary judgment ruling that property owner, R&D and tenant, Spartan Stores, Inc., were not negligent in failing to provide sufficient security at the grocery store run by Spartan Stores, resulting in an assault on Appellant Krause. The Court reviewed the case *de novo* and upheld the lower court's holding. To prove negligence, Appellant needed to show that defendants had a duty, that duty was breach, and causation. In determining the case against the landlord, the first issue was whether a duty existed for R&D. The Court found that R&D did not have control of the premises and therefore had no duty to the Appellant. In reaching this conclusion, the court noted that Spartan was in possession of the property, and further that for control to exist, an entity must have both the right or power to admit or exclude persons from the premises, as well as a "substantial exercise of that right and power". The court found that although R&D had the power to exclude, it did not exercise that power, as acting as only landlord and not tenant in control, and as such had no duty.

Tenant Spartan Stores was deemed to not be negligent on the grounds that they had no duty because the crime was not foreseeable. Appellant offered reports of crime in the area that the Court deemed did not give sufficient notice, and expert testimony failed to show forseeability of the crime. As such, the Court upheld the lower court's ruling.

LANDLORD/TENANT; LANDLORD'S REMEDIES; DAMAGES: Where, instead of reletting abandoned premises, landlord operates the business on the premises and does so profitably, landlord may still collect from abandoning tenant the difference between the market rental value of the premises and, if higher, the contract rent under the abandoning tenant's lease. ***Lu v Grewal (2005) 130 CA4th 841, 30 CR3d 623 2005)***,

Tenant entered into a long term lease for a mini mart/gas station location in Los Angeles. The lease required that the tenant maintain the premises in good condition and repair. Tenant assigned the lease, but did not obtain a release from the landlord, and remained liable for its performance. Later, the assignee abandoned the premises and stopped paying rent. Landlord, during the term of the lease, had purchased the fixtures and equipment on the premises from an oil company for about $800,000. When Landlord came to the premises, the abandoned facility had been thoroughly vandalized. The gas pumps and related equipment were gone. There remained only holes in the ground above the oil tanks. The mini mart was in a shambles and the cash register and other valuable fixtures gone.

Landlord restored the premises and, through dint of extraordinarily hard work outlined by the court, managed to make the business profitable. Years passed while the rent remained unpaid. Eventually, Landlord sued the original Tenant for the cost of restoration and for the rent.

California has codified the concept of the landlord's duty to mitigate rent following tenant abandonment. Under CC §1951.2, the lease ended when the tenant abandoned and the time stated in the landlord's notice to quit expired; this established the landlord's recovery as the difference between the rent reserved under the lease and the rental value of the premises for the remainder of the term. Landlord can collect in one claim the past damages, with interest, and future damages, reduced to present value.

We only have the appellate court's explanation of the facts But, based on those facts, the tenant then showed the incredible *chutzpah* to argue that the landlord was obligated to prove that it had not recovered from the property the amount of the rent, and that the landlord had to credit the profits that it had earned in mitigation of the rent obligation. And not only that – the trial court had the *chutzpah* to agree with the tenant!!! And, since the tenant already had agreed to pay the damages for the ruination of the premises, the trial court ruled that the landlord had not prevailed, so the tenant got attorney's fees.

On appeal: *Held: reversed.*

The court ruled, first, that California statute should be read to place the burden of showing any mitigation credit on the tenant, not the landlord. Second, the California statute does not require that any monies the landlord obtains from use of the premises be credited, but only the reasonable rental value of the premises during the landlord's occupancy for the balance of the term.

Remanded for a redetermination of the proper damages and, if the landlord was entitled to a recovery, a redetermination of whether the landlord should get fees.

Reporter's Comment 1: So, if the rent reserved under the lease was $5000 a month, but the rental value of the premises was only $4000 a month at the time of abandonment, the landlord is entitled to a rental loss of $1000-5000 less 4000-times the number of months left under the lease, adjusted upward for interest on months prior to trial and discounted for future value on the months left after trial, until the termination date of the lease. This formula puts a *de facto* duty to mitigate on the landlord, since if her tenant is going to be credited for what she could have relet the premises, it is too dangerous not to try to get that much money herself from a replacement tenant. At the same time, the burden of proving all this is on the tenant, who also has the *de facto* opportunity to mitigate his liability by finding and proffering a ready and willing replacement (which the landlord rejects at its peril).

Reporter's Comment 2: Thus, the "operational profits" and "sale valuation" used by the experts in this trial were out of place and should never have been admitted into evidence. In general, the landlord's retaking possession does make determination of rental value less subject to the landlord's control. On the other hand, if the landlord believes that it has no real choice but to go back into possession, and operate, it might be better off in creating a new entity and executing the new lease with it, on terms that, while favorable, are not so far out of line as to be rejected out of hand. (If the old tenant wants to match or beat those terms with his own candidate, all the better.)

In general, the landlord's retaking possession does make determination of rental value less subject to the landlord's control. On the other hand, if the landlord believes that it has no real choice but to go back itself, landlord might be better off in creating a new entity and executing the new lease with it, on terms that, while favorable, are not so far out of line as to be rejected out of hand. (If the old tenant wants to match or beat those terms with tenant's own candidate, all the better.)

Also see: Millikan v. American Spectrum Real Estate Services, Inc., 2004 WL 837210 (Cal. App. 4/20/04), the DIRT DD for 4/29/04, (California landlord can claim as mitigation the cost of selling the premises following tenant's abandonment, without taking into account any profit made on resale, when selling the premises was a rationale response to the tenant's abandonment of a whole building in a down market.

The Reporter for this item was Roger Bernhardt of the Golden Gate Law School in San Francisco, writing in the California Real Property Reporter. The editor has substantially rewritten the whole item, but the ideas in the comments are Roger's.

LANDLORD/TENANT; LANDLORD'S REMEDIES; DAMAGES; DUTY TO MITIGATE: Landlord satisfies duty to mitigate by offering premises for sale through a broker at price premises has rented for during rentals over the previous seven years. There is no requirement that landlord offer premises for lease at any price. ***Thomas & Kline Realty Co. v. George Rogers, Court of Appeals No. L-04-1361, 2005 Ohio 4876; 2005 Ohio App. LEXIS 4423 (9/2/05)***

Tenant left the leased office premises and stopped paying rent four months before the end of the lease term, sending landlord a letter that he was vacating prematurely. Landlord listed the premises with a reputable broker, and indeed it was shown to several prospective tenants, but not rented until after the lease had expired. Landlord sued for the four months unpaid rent, and tenant objected on the grounds that landlord should have leased the premises for whatever they would bring, instead of setting a rent at the price for which the premises had been renting over the prior seven years.

As the caption indicates, the court didn't buy tenant's argument. It noted that the controlling Ohio Supreme Court authority, although it had not discussed the price element of a mitigation, had noted that landlord has no obligation to rent to "just any old tenant." Consequently, the landlord behaved properly in offering the premises for rent at a reasonable price based upon the historical market.

Comment 1: Sometimes these cases are about something other than what the appellate decision reveals. Tenant's proposition on its face seems absurd: why should the landlord, presumably looking for a longer term than four months, be required offer the premises at a bargain price just to protect the defaulting tenant?

Comment 2: At the same time, there's a lesson here. Well advised landlord will put into the lease language protecting specifically their reasonable business decisions when acting to mitigate. The language should state expressly what the landlords are able to do (without limitation) in terms of new term, combination with other space, limitations on use and other matters, and, of course rent. Courts normally will uphold such language if at all reasonable, and the landlord won't be faced with nit picking appeals.

LANDLORD/TENANT; LANDLORD'S REMEDIES; DAMAGES; HOLDOVER: Although landlord shows that tenant wrongfully retained possession of the premises for a substantial period beyond the lease term, landlord has burden of showing that the holdover caused it injury, and court will not assume existence of lost profits. ***Lay Bros., Inc. v. Golden Pantry Food Stores, Inc., 273 Ga.App. 870, 616 S.E.2d 160 (2005).***

Tenant continued in possession of the premises for a substantial period of time and landlord was delayed ten months following the end of the lease term in its rehabilitation of the premises for its own uses. The delay apparently was due to delays in removing their fixtures and the completion of environmental cleanup. Reading between the lines, however, there appeared to be another motive as well. Landlord was an assignee of the original landlords and operated a convenience store business that was in competition with tenant's other locations. Perhaps tenant was in no hurry to permit Landlord to get established at this location.

The Court of Appeals of Georgia restricted the Plaintiff's recovery to nominal damages where the Plaintiff suffered obvious harm due to the Defendant refusing to surrender the premises, but the Plaintiff presented no evidence of damage, and only speculated as to the amount of such damages.

Comment: The landlord claimed that it should have been permitted to show damages after a ruling that the court made on the validity of an assignment to the landlord. The court concluded that it was procedurally barred at this point. But, in any event, it noted that lost profit damages are exceedingly hard to show in any event.

LANDLORD/TENANT; LANDLORD'S REMEDIES; FED ACTION; PROCEDURE; *RES JUDICATA:*. Lease/Purchaser's claim for, *inter alia*, breach of land sales contract was barred by *res judicata* as a compulsory counterclaim that ought to have been filed in response to vendor's earlier forcible entry and detainer action brought in capacity as landlord. ***Forney v. Climbing Higher Enterprises, 815 N.E.2d 722 (Ohio App. 2004)*** , discussed under the heading: "Vendor and Purchaser; Procedure; *Res Judicata."*

LANDLORD/TENANT; NOTICE: Where tenant has right to claim abatement of rent upon "immediate" notice to landlord of injury to premises affecting tenant's occupancy, tenant's obligation to provide notice is not governed by general provision requiring that all notices from tenant by landlord be by certified or registered mail. ***Ring v. Arts International, Inc., 7 Misc. 3d 869, 792 N.Y.S. 2d 296 (N.Y. Civ. Ct. 2004)***

Tenant claimed that it was entitled to abate rent when the sprinkler system in its premises malfunctioned, dousing the area. The lease stated that if the premises were damaged by "fire or other casualty" tenant was to give landlord "immediate" notice. Then, the same provision in the lease stated that if the premises were rendered wholly unusable, then rent completely abated until Landlord effected a repair of the condition. When the sprinkler damage occurred, Tenant sent to Landlord a letter by regular mail stating that the premises had been rendered untenantable and that it was withholding rent.
Landlord disputed that the premises were rendered untenantable. When Tenant failed to pay rent, Landlord sued for possession, and Tenant defended on the grounds of the abatement right set forth in the lease.

One of the issues in the case was whether Tenant had properly invoked the right by mailing notice to the Landlord. Another part of the lease stated that "Except as otherwise in this lease provided. . . Any notice by Tenant to Owner must be by registered or certified mail . . . ." It was conceded that Tenant had not sent the notice by registered or certified mail.

The court first noted that the Landlord admitted that it had received the letter. It stated that the law was clear that where Landlord responds to a notice, demonstrating that it has received the notice, its failure to object promptly to the form of notice is a waiver of its right to assert that the notice was invalid.

But the court's second holding on the point is important to note. It held that the lease paragraph providing for casualty, by providing for "immediate notice" demonstrated that the parties did not intend that the "certified or registered" mail requirement apply. The court noted that the notice provision stated expressly that it these requirements applied "except as otherwise in this lease provided," and in this case the lease did provide otherwise.

Comment 1: The editor views that court's analysis of the notice requirement as not logical, although he cannot quarrel with the outcome as applied to these facts. Why should the requirement for "immediate notice" preclude use of registered or certified mail? Registered or certified mail might provide greater certainty of notice. Isn't the landlord entitled to that? What if the tenant's mailed notice had not reached the landlord at all. Was it nevertheless valid when mailed "immediately?"

Comment 2: Obviously there's a drafting lesson here that might have more teeth in it in other circumstances. You can't rely upon a general statement of notice requirements if arguably there is detail about the form of notice elsewhere in the lease. Either refer over or cover all notices of any kind in a single provision.

LANDLORD/TENANT; LEAD PAINT: The City of New York owes no special duty to children who have been exposed to lead paint in an apartment owned by the City. ***Peri v. City of New York, 798 N.Y.S.2d 332 (Sup. 2005).*** Three children were exposed to lead paint at residences owned by New York City. The amount of exposure was below the threshold level considered by the Center for Disease Control to be "normal," but the Court held that the claim was actionable.

The Court also held, however, that the City owed no special duty to children exposed by lead paint, nor was it liable for the operation of the building as it was statutorily exempt from liability related thereto. Therefore, the only possible claim against the City is for negligence in failing to abate the levels of lead paint.

LANDLORD/TENANT; PREMISES: Where the terms of a lease clearly establish that "premises" refers to interior building space, extrinsic evidence cannot be admitted to show that environmental contamination outside of the interior space was covered by the "yield up" clause require that premises be delivered in good order and condition, even when the lease consisted of an entire building. ***South Road Assoc., LLC v. IBM, 826 N.#. 2d 806 (N.Y. App. Ct. 2005)*** This affirms the lower court case that was the DD for 5/3/04. The editor commented as follows:

> 'A classic conundrum. The dissenting judge may very well be correct that the lawyer who wrote (or inserted) the language in the "yield up" clause was not thinking about the more restrictive definition of the word "premises" appearing elsewhere in the lease. If that lawyer did not think of it, none of the laypersons reading the lease would ever catch the problem. Thus, it is quite likely that the parties signing the lease many decades ago in fact expected that the tenant had the responsibility to return the whole property in good condition.
>
> But these were sophisticated parties represented undoubtedly by people whom they trusted for their competence in the lease negotiations, and the best interests of the marketplace usually are served by requiring parties to live with the outcome of the language that they select. There are devices that expensive lawyers doing important documents often use to test that a defined term is properly used throughout the document. Often this seems like needless overkill, but the investment is appropriate to avoid consequences such as those occurring here."

LANDLORD/TENANT; QUIET ENJOYMENT; PHYSICAL INTRUSION: New York court sanctions *de minimus* physical intrusion by landlord into tenant's space. ***Eastside Exhibition Corp. v. 210 E. 86th St. Corp.,2005 Westlaw 2233306, 2005 NY Slip Op 06735 N.Y.App. (1st Dept. September 15, 2005 Appellate Division).***

Tenant rented "between 16,000 and 19,000" square feet of space (why don't we know exactly?) used as a four theater movie house in Manhattan. The lease permitted landlord to enter the premises to make repairs and improvements at reasonable times, and provided that there would be no diminution of rent for such intrusions.

Landlord resolved to add two additional stories to the building. Without prior notice or permission, Landlord entered Tenant's space and constructed steel crossbeams between pillars in the tenant's space. The crossbeams did interfere some with traffic in the tenant's space, but the interference was not great, as the crossbeams collectively occupied only twelve square feet of space. Landlord announced intentions to install additional crossbeams. Tenant went to court for an injunction and immediately commenced withholding rent, relying on the traditional rule in New York and elsewhere known as the "one inch" rule – that a physical intrusion of any part of the premises justifies a 100% abatement in rent.

The "one inch" rule is based upon venerable precedent in New York. It first appeared there in 1827 at the latest, and is part of earlier English Common Law. "'[N]o man may be encouraged to injure or disturb his tenant in his possession, whom, by the policy of the feudal law he ought to protect and defend." No less an authority than Judge Cardozo upheld the rule in several cases, because "a landlord is not permitted to apportion his own wrong."

The trial court granted the injunction and upheld the withholding of over $830,000 or rent for the invasion.

The Appellate Division reversed. It held that the "one inch" rule is an outmoded relic of an earlier time.

> "In light of current landlord/tenant realities and policies, it appears particularly untoward automatically to apply harsh and oppressive strictures derived from feudal law that mirror the policies and concerns of that earlier society. Instead, we conclude that a more realistic remedy than total rent abatement should be imposed for a partial eviction of the minimal proportions here present."

The court dissolved the injunction and remanded the case for further hearings on the amount of injury suffered by the landlord for the continuing invasion of its premises by the steel beams.

Comment 1: What!!??? What!!!!!??? That's right – right at the end, with hardly a whisper of warning, the court not only sets aside the one inch rule, which probably has outlived its usefulness as a remedy for landlord invasions of space, but also holds that the landlord's unpermitted physical invasion may continue. This last part of the holding comes out of nowhere. The court shows no understanding of the difference between finding *de minimus* damages for a *de minimus* physical invasion and the much more significant proposition that courts will not longer protect the physical boundaries of the possessor of land through injunction.

Comment 2: This case is very fresh. The editor urges the New York leasing bar to seek an *amicus* appearance and encourage an appeal to reestablish the very important principle that landlords cannot invade leased space with impunity any more than anyone else can – *de minimus* consequences or not.

Comment 3: As for the "one inch" rule – the editor was surprised to learn that some authorities are of the view that is the general rule still in America, Stoebuck and Whitman, in their hornbook on Property law, talk about the doctrine as alive and well, although they note that that the landlord cannot apportion his wrong as a rationale that is "talismanic as opposed to rational." Sec. 6.32. In fact, Stoebuck and Whitman talk about a controversy as to whether in fact the tenant can do more than withhold rent – they indicate that some authorities would give the tenant the option to rescind the lease entirely. This also seems over the top where the invasion is *de minimus*, but only if ultimately the invasion is removed.

Friedman on Leases, on the other hand, discusses the doctrine only in a buried footnote, but there asserts that "partial actual eviction suspends the rent only if a substantial part of the premises is taken, citing California and New York cases. (Sec. 3.1 note 13.)

The editor agrees that it seems appropriate to treat an actual eviction as giving rise only to apportionable damages, but feels that it ought to be treated also as a tortious trespass, with appropriate punitive damages where (as, possibly in this case) the injury is knowing, deliberate and sustained. See, generally, the extensive discussion of the trespass remedy as an alternative to breach of contract set forth in Friedman on Lease Section 29.4.

The court here would sanction the landlord's simply moving in for its own convenience and redoing the lease on a "no harm, no foul" rationale. New York leases have been removed from their status as property and have been reduced to mere contracts.

New York Bar – get busy!!! This is wrong.

LANDLORD/TENANT; PREMISES: Where the terms of a lease clearly established that "premises" referred to interior building space, extrinsic evidence could not be admitted to show that environmental contamination at the site violated a "good order and condition" clause. ***South Road Associates, LLC v. International Business Machines Corporation, 826 N.E.2d 806 (N.Y. App. Ct. 2005).***

In 1981, Landlord renewed a lease with International Business Machines Corporation ("Tenant") for a property Tenant had occupied for over twenty years. Tenant used the property for manufacturing and commercial operations, and during its occupancy Tenant installed an underground storage tank to hold chemical waste. Tenant discovered that the tank had leaked, contaminating the site's groundwater and soil, and had undertaken remedial efforts.

In 1984, Tenant and Landlord entered into an agreement whereby Tenant acknowledged responsibility for the contamination, agreed to abate it "to the satisfaction of all requisite governmental agencies," promised to hold

Landlord harmless for any resulting claims, and additionally promised to restore the land to its previous condition.

In 2000, six years after the termination of the lease, Landlord sued Tenant, not for breach of the 1984 agreement, but rather for breach of the lease provision requiring that the premises be returned to Landlord in "good order and condition." Landlord claimed that the soil, groundwater, and bedrock contamination violated this provision of the lease. The Supreme Court granted partial summary judgment for Landlord on the issue of liability for the claimed breach, finding that extrinsic evidence showed the leasehold covered by the lease extended beyond the lease's definition of the word "premises" with reference to an attached floorplan.

The Supreme Court Appellate Division reversed, finding that the clear language of the lease established the premises as the buildings' interior space. The Court of Appeals affirmed the Appellate Division's findings, noting that the instrument was negotiated by sophisticated parties and that the negotiated language established "premises" as only the interior space. The lease treated "premises" as conceptually distinct from a water tower, appurtenances, land, a parking lot, and the buildings themselves. The court held that it was inappropriate for the trial court to consider extrinsic evidence where the lease itself was not ambiguous, and accordingly, the order of the Appellate Division was affirmed.

Comment: The lower appeals court opinion was the DD for 5/3/04.

LANDLORD/TENANT; RENT: A mistake in the "stipulated" base rentable area of a lease is a mutual mistake by the parties, and prejudgment interest should be awarded in connection with judgments arising out of a contract or other transaction. ***Local Marketing Corp. v. Prudential Insurance Co. of America, 824 N.E.2d 122 (Ohio App. 2004).***

Prudential, as landlord, and Local Marketing Corporation ("Tenant") entered into a commercial office lease in February of 1998 for office space in downtown Cincinnati. The lease stated that the base rentable area would be "stipulated for all purposes to be approximately 5,845 square feet". Some three years later, Tenant discovered that the actual size of the property was roughly 8% smaller than the lease indicated. Tenant sued on several theories, and received judgment under the doctrine of mutual mistake.

Tenant was awarded overpaid rent, and Landlord was awarded overpaid build-out expenses, which had been determined based on square footage. The Appeals Court upheld the ruling, finding that neither the words "for purposes" nor "approximately" established that the parties intent under the contract was anything other than a lease covering the square footage indicated. Both parties indicated that had the correct number been known at the time, it would have been included in the lease. Financial considerations for each side were based on the square footage, clearly rendering the mistake material.

The trial court had not ordered prejudgment interest to either party. Under Ohio law (R.C. 1343.03(A)), prejudgment interest attaches to all "judgments, decrees, and orders of any judicial tribunal" where payment is required for "tortious conduct or a contract or other transaction". The court found that money "directly due and payable under a contract" should include prejudgment interest in order to fully compensate the aggrieved party. Such a contractual award leaves no room for discretion on the part of the trial court.

The appeals court found that, as the mistake was mutual, neither party had been made whole by the trial court's awards, which lacked prejudgment interest. Therefore, Tenant was entitled to prejudgment interest on its award for overpaid rent, and Landlord was entitled to prejudgment interest on its award for overpaid build-out expenses. In both cases, the interest should be calculated from the time the payments were made rather than from the time the suit was filed. The court affirmed in part, reversed in part, and remanded for further proceedings.

LANDLORD/TENANT; RESIDENTIAL; RENT CONTROL; NON-RENEWAL; WAIVER: A landlord waives its right to bring a holdover proceeding when it cashes a rental check. ***Metropolitan Ins./Annuity Co. v. Rowinsky*, 798 N.Y.S.2d 320 (N.Y.City Civ.Ct. 2004).** A landlord sent a tenant a notice of non-renewal. The landlord then billed the tenant for a rental period beyond the termination date and accepted and cashed payment. Upon realization of its mistake, the landlord returned the tenant's money. The landlord claimed it "inadvertently" accepted the rental payment and therefore, even though it accepted the rental payment, it did not vitiate the non-renewal notice and hence did not waive its right to bring a holdover proceeding. The Court held that since the landlord affirmatively billed the tenant for rent and, when returning the rental payment, only stated that it "inadvertently" accepted the funds (without further explanation), the landlord waived its right to bring a holdover proceeding.

LANDLORD/TENANT; RESIDENTIAL; WARRANTY OF HABITABILITY:. Each townhouse in a complex of townhouses is a separate building for the purposes of exemption from the provisions of the Chicago Residential Landlords and Tenants Ordinance. ***Allen v. Lin, 826 N.E.2d 1064 (Ill. App. Ct. 2005).***

Plaintiff tenant and defendant landlords lived in townhouses owned by the landlords. The townhouses were two units away from one another and were located under one roof. Tenant brought action against landlords for breach of contract and violations of the City of Chicago Residential Landlords and Tenants Ordinance (Chicago Municipal Code § 5-12-101 *et seq.* (2004)) (RLTO).

At the bench trial, the circuit court granted the defendants' motion for directed verdict on the RLTO claims on the grounds that section 5-12-020(a) of the RLTO exempted the property in question from application of the ordinance. The exemption applied to "owner-occupied building[s] containing six units or less." The trial court relied on the defendant's testimony that the tenant's unit and the landlords' unit were among six units located "under one roof" to determine that these six units comprised a "building" for the purposes of the exemption. The trial court rejected plaintiff's argument that townhouses should be considered separate buildings just as if they were single-family homes, even if they are under one roof.

Plaintiff argued on appeal that the court erroneously applied the RLTO exemption to the premises. However, the appellate court reversed the trial court's decision as to the application of the RLTO and remanded for further proceedings. Relying on a principle elucidated in *Meyer v. Cohen*, 632 N.E.2d 22 (Ill. App. Ct. 1993), the only case in Illinois to have interpreted the "owner-occupied" exclusion of the RLTO, the appellate court argued that section 5-12-020(a) must be interpreted in a way that is logical, that gives effect to the legislative intent and that protects public interests. The court then looked to the stated purpose of the RLTO "to establish the rights and obligations of the landlord and the tenant in the rental of dwelling units," and to *Sandstrom v. De Silva*, 645 N.E.2d 345 (Ill. App. Ct. 1994), where the court held that each townhouse in a group of townhouses constituted a separate building for the purposes of Chicago Municipal Code section 13-4-010. In light of these considerations, the court found that each townhouse constitutes a separate building for the purposes of the RLTO.

Comment: Although the opinion does not say so, presumably the Act would not apply if there were six units in a row of townhouses and the entire complex was owned by a resident landlord. The concurrence states that it was the legislative intent to establish a different rule where the landlord resided in the same building as the tenant. How could this be different if the units are apartments or townhomes?

LANDLORD/TENANT; TENANT'S REMEDIES; RENT WITHHOLDING; PHYSICAL INVASION: New York discards "one inch" rule – damages from landlord's physical invasion of premises must be apportioned, and tenant cannot withhold entire rent. ***Eastside Exhibition Corp. v 210 E. 86th St. Corp., 2005 Westlaw 2233306, 2005 NY Slip Op 06735 N.Y.App. (1st Dept. September 15, 2005 Appellate Division),*** discussed under the heading: "Landlord/tenant; Quiet Enjoyment; Physical Intrusion:"

LANDOWNER LIABILITY; SOVEREIGN IMMUNITY; PUBLIC WAYS: A city is responsible to keep safe not only public ways but also areas immediately around those ways, including areas that are part of a public park, and will be regarded as engaged in a proprietary, rather than governmental, function, in doing so. Therefore, sovereign immunity will not apply, even though such immunity normally does apply to failure to maintain properly a park. ***Whalen v. Mayor of City Council of Baltimore, No. 99862, 2005 WL 2242172 (Md. App. 9/16/05)***

The opinion starts with the statement: "This appeal gives new meaning to the phrase: 'an accident waiting to happen.'" Needless to say, it was all downhill from there from the standpoint of municipal liability.

Here's the setup – a hole nineteen inches square and nearly four feet deep is located in a grass area (mowed) a few feet from a streetside sidewalk and adjacent to a fence in a city park. The hole is the former site of a foundation for an electrical transformer. It had a cover, but the lip for the cover had rusted away and the cover sat in the bottom of the hole. From appearances, the hole likely had been that way for several months. Across the street from the park is an office of the National Federation of the Blind, and people in the National Federation routinely tell blind visitors they can use the park to let their guide dogs relieve themselves.

Plaintiff, who is blind, took her guide dog to the area and, letting him roam a bit in the grass, fell into the hole and permanently disabled herself.

The trial court granted summary judgment to the City on the basis of the City's sovereign immunity.
On appeal: *Held: Reversed.*

Sovereign immunity in Maryland seems to be a creature of common law (the case cites no sovereign immunity statute.) Although the City does enjoy sovereign immunity for its governmental functions, it does not enjoy such immunity for proprietary actions, unlike State government. The maintenance of parkland is viewed as governmental in character. Apparently this was the basis for the trial court's ruling.

But the intermediate appeals court ruled that the area where the hole was located was sufficiently close to a public street and sidewalk to be viewed as within the proprietary liability of the municipality. In a precedent case, a court had found a city liable for injuries occurring on a walkway in the public park that ran between two streets. Plaintiff was injured while crossing from one street to another. In a second precedent case, Plaintiff's decedent perished when city employees in a public square negligently let a rotten tree limb fall on her while she was walking on a public sidewalk adjacent to the square. Again, sovereign immunity did not apply.

The critical analysis in the case was the conclusion that once a particular site was shown to be potentially dangerous to persons making use of the public road or sidewalk, the City had a duty to maintain it in safe condition for anyone who went upon it, whether or not they were going on the area to make use of park functions, as arguably the plaintiff was in this case, or going on it in connection with use of the nearby public right of way.

Once this conclusion was reached, of course, it was a simple matter to conclude that the question of sovereign immunity could not be decided against plaintiff on summary judgment. The court remanded to case for a factual determination below as to whether the area where the hole was located was sufficiently closely related to the adjacent sidewalk to justify the conclusion that it was effectively part of the street. Although the trial court conceivable could say no, the editor virtues a guess that it could do so only at its peril to this court.

Comment: This is the first sovereign immunity case DIRT has reported. The editor isn't aware how much Maryland law in this area has in common with other states, but he knows that the proprietary/governmental distinction does arise. Of course, from the beginning, this case was result oriented, but as precedent it does present some issues for those representing local governments to take into account. The notion that the park adjacent to the roadway is part of the roadway for liability purposes might lead to advise to install barriers dividing the two uses. Of course, the barriers themselves could become the source of liability. Oh, well. At least insurance is cheap. Ooops!!

LIS PENDENS*; FRAUDULENT CONVEYANCE:** A *lis pendens* will be invalidated in the absence of an alleged right to attachment or other encumbrance. ***Shrewsbury v. Seaport Partners Limited Partnership, 826 N.E.2d 203 (Mass. App. Ct. 2005).

Trustees of the Seaport Condominium at Marina Bay (the "Condominium") filed suit against the Developer, its General Partner"), and Initial Trustee (collectively, the "Defendants"). The Trustees alleged various construction defects and further alleged that ownership of eight units in the Condominium was transferred from the Developer to entities controlled by Mitchell B. Robbins, who was a principal in both the General Partner and the Developer, for the purpose of defrauding creditors such as the Trustees.

Along with other actions, the Trustees moved for authorization to record a memorandum of *lis pendens*. The Superior Court ruled that a fraudulent transfer claim does not qualify under the *lis pendens* statute, G.L. c. 184, § 15. The Trustees filed an interlocutory appeal. The appeals court found that G.L. c. 184, § 15 allows the recording of a memorandum of *lis pendens* only where the proceeding "affects the title to real property or the use and occupation thereof." Here, the Trustees' claim was that they might have the right to cause the property to be reconveyed back the Developer at a future date in order to satisfy a judgment. They did not have any actual attachment or encumbrance, and thus were not in a position to move in advance for enforcement. The Superior Court's ruling was upheld.

LIS PENDENS;* REQUIREMENT OF PENDING ACTION*: *Lis pendens* may be filed only in a proceeding affecting title to real property or use and occupation thereof It is not available for a fraudulent transfer claim. ***Shrewsbury v. Seaport Partners Limited Partnership, 826 N.E. 2d 203 (Mass. App. 2005).***

MORTGAGES; ASSIGNMENT; MERS: Florida trial court rules that MERS lacks status to foreclose as representative of lender even when MERS holds the note. ***In re Mortgage Electronic Registrations Systems, Inc., Cir. Ct. Pinellas County, Fla., Walt Logan, Judge, 8/18/05) (Numerous case numbers)***, discussed under the heading: "Mortgages; Foreclosure; Procedure; Standing to Foreclose."

MORTGAGES; DEFICIENCIES; CHOICE OF LAW: If a foreclosure occurs in another state, which does not require judicial confirmation in order to collect a deficiency, and the rights are assigned to a bank in a state (Georgia) that does require such confirmation, the bank is not required to get judicial confirmation of foreclosure sale in accordance with its own state's law before seeking deficiency judgment in its own state. ***Graham v. Casa Investments Co., 274 Ga.App. 59, 616 S.E.2d 833 (2005).***

The court commented that the dispositive question was not where the mortgage defendant resided, but rather where the contract was made.

Comment: Thus, the court does not seem to be of the view that the *situs* of the foreclosure was critical. Does this mean that if a Georgia resident borrowed money in Alabama from an Alabama bank and the loan was secured by Georgia property, there would be no requirement for a judicial confirmation before the Alabama bank could pursue a deficiency? The editor suspects that the answer to this question is "no" and that the court has perhaps overstated its emphasis on the *situs* of the contract. (Unless all mortgage loans secured by Georgia property are by definition sited in Georgia.)

MORTGAGES; FORBEARANCE; CONSIDERATION: Payment of outstanding loan balance is insufficient consideration to support a contract to forego foreclosure. ***Citizens Trust Bank v. White, 618 S.E.2d 9 (Ga. App., 2005).***

Borrower had prevailed below in a suit against Lender for breach of a contract to forbear. It awarded $250,000 in actual damages (suggesting that this was the amount of value the jury thought was lost at foreclosure) but no punitive damages.

Apparently the amount of the mortgage debt was only about $40,000. There was some question about application of insurance proceeds in that amount to rebuilding, but it does not appear that this issue had much to do with the outcome here.

Borrower had missed several payments, and bank scheduled the property for foreclosure. Borrower repeatedly blocked the foreclosure with bankruptcy filings for two years, and each filing was dismissed. He finally was enjoined from filing any further bankruptcies. The parties then entered into a letter agreement that provided that Bank agreed to "postpone the foreclosure" if Borrower would pay $35,000 to Bank on the (apparently accelerated) debt. The letter stated that there would be a remaining unpaid balance of approximately $5,000. There was no provision for when that would be paid, but Bank testified that it expected payment of the balance within another thirty days.

Borrower made the payment and the foreclosure was postponed. Borrower stated that he expected a letter detailing the application of the $35,000. (Note that the original letter agreement stated the precise amount that would still be owing).

The forbearance agreement letter was signed May 7. On July 24 of the same year, Bank sent Borrower another notice of foreclosure. It completed the foreclosure in September by bidding in the $5000 debt plus interest, a total of $5,986.

The Court of Appeals did not enforce the contract because of lack of consideration. Though Bank's act of forbearance constituted adequate consideration for a contract, Borrower's payment of a debt that he already owed was not sufficient consideration for a contract.

Comment: If indeed, the lost equity in this foreclosure was $250,000, as found below, the editor would have expected more discussion of alternatives to the requirement of consideration, such as promissory estoppel. Perhaps the court concluded that the statement of remaining indebtedness in the letter agreement was sufficient to put the Borrower on notice that he had to promptly clear up the balance of the debt, but surely one should expect greater clarity from a bank in dealing with a borrower under these circumstances.

On the other hand, there likely was not much uncertainty about the notice of foreclosure. Perhaps the court concluded that the Bank, overall, had been patient enough.

MORTGAGES; FORECLOSURE; INSURANCE: When a fire causes damage to a foreclosed property during the redemption period but the deed is erroneously delivered during that time, the insurance proceeds are to be paid to the foreclosing lender to the extent of the debt and the borrower is entitled to a credit for the value of the property received in the foreclosure sale. ***Liberty Mutual Fire Insurance Company v. Alexander, 374 N.J. Super. 340, 864 A.2d 1127 (App. Div. 2005)***, set forth in under the heading: "Mortgages; Insurance; Statutory Redemption."

MORTGAGES; FORECLOSURE; POSSESSION. Illinois foreclosure law requires that possession orders specifically name occupants; and otherwise sheriff may refuse to execute. ***Fairbanks Capital v. Coleman, 816 N.E.2d 695 (Ill. App. 1 Dist. 2004)***.

In April 2002, plaintiff mortgagee filed a mortgage foreclosure action pursuant to the Illinois Mortgage Foreclosure Law (the "Foreclosure Law") (735 ILCS 5/15-1501 et seq. (West 2002)). The trial court entered a judgment of foreclosure in August 2002, and in December 2002 the court entered an order approving the foreclosure sale and a possession order. The possession order named only Celestine Moore.

In March of the following year, the plaintiff mortgagee filed the complaint in the instant case pursuant to the Illinois Forcible Entry and Detainer Act (the "Detainer Act") (735 ILCS 5/9-101 et seq. (West 2002)), naming Stanley Coleman, Stanley Walson, and "Unknown Occupants" as defendants. In April, the trial court entered a default order in favor of the plaintiff mortgagee seeking possession, stating in the order that the court found that unknown occupants were properly named and properly served.

When the sheriff arrived at the premises to execute the order, two occupants were present who had not been specifically named in the possession order. Based on this discovery, the sheriff refused to enforce the possession order, and plaintiff subsequently filed a petition for a rule to show cause why the sheriff should not be held in contempt for such refusal. Following a hearing, the trial court found the sheriff in indirect civil contempt for failing to carry out the eviction of the two unnamed occupants. The sheriff's office appealed the order.

Plaintiff argued that the occupants were named with sufficient specificity to satisfy the requirements of the Detainer Act. The court observed that there was an apparent conflict between the Foreclosure Law and the Detainer Act; the former provides that an order of possession "shall not be entered and enforced against any person who is only generically described as an unknown owner." (Foreclosure Law, supra, at § 15-1508 (g)), while the latter authorizes possession orders against generically named occupants on the premises (Detainer Act, supra, at § 9-104).

Plaintiff argued that the two statutes provide independent bases of relief; the sheriff argued that the Foreclosure Law preempts the Detainer Act where an order is sought under the Detainer Act within ninety days after obtaining orders of foreclosure and possession for the same premises pursuant to the Foreclosure Law. The court noted that the plain language of the Foreclosure Law provides that it "shall supersede any other inconsistent statutory provisions," (Foreclosure Law, supra, at § 15-1701 (f)) and that it is a fundamental rule of statutory construction that a specific statutory provision controls when there is an apparent conflict with a more generic statutory provision. *Knolls Condominium Ass'n v. Harms,* 781 N.E.2d 261 (2002). The court held that the right to seek relief under the Detainer Act is limited by the provisions of the Foreclosure Law when that relief is sought within ninety days of the initial order of possession in the foreclosure action. The trial court's contempt judgment was vacated and remanded for further proceedings.

MORTGAGES; FORECLOSURE; PROCEDURE; STANDING TO FORECLOSE: Florida trial court rules that MERS lacks status to foreclose as representative of lender even when MERS holds the note. ***In re Mortgage Electronic Registrations Systems, Inc., Cir. Ct. Pinellas County, Fla., Walt Logan, Judge, 8/18/05) (Numerous case numbers)***

As most readers of this list know, the Mortgage Electronic Registration System, MERS, was established about fifteen years ago to facilitate the rapid transfer of mortgages for the purpose of developing large pools to support securitization of mortgages. All parties participating in the MERS system (primarily mortgage bankers) agree to recognize as the owner of a note and mortgage that party shown on the MERS register. Although, originally, MERS functioned without recording and without taking possession of the note, more recently MERS has both recorded itself as the record owner of the mortgage at the time of the original loan funding, or shortly thereafter, and has also begun to take possession of a note endorsed in blank.

One assumes that the various parties who rely upon MERS as the registry of ownership of mortgage loans that they make sign agreements that make very plain the powers that MERS has to foreclose in their name. Use of MERS has become the standard for residential mortgages, over 95% of which are securitized, and for securitized commercial mortgage as well. But this Florida case puts at least MERS' foreclosure arrangements very much at issue.

This order dismissed foreclosures in 28 pending foreclosures brought by MERS in Pinellas County. In each case, MERS was listed as a plaintiff or co-plaintiff seeking to collect on a note via mortgage foreclosure. In the end, the court dismissed all 28 cases for want of a proper party plaintiff.

In each case, MERS acknowledged that it was representing the interest of another corporate entity in the collection effort, and described its role as a "nominee" of the other corporate entity.

The court reviewed the files and stated that it found that the petition for foreclosure, which alleged that MERS "now owns and holds the mortgage note and mortgage" were not supported in the record. It acknowledged that MERS claimed that it was a "nominee" or the corporate entity that owned the note, but claimed that one corporation is not permitted to act for another in bringing a lawsuit. Rather, lawyers, and not corporations, represent other corporations in lawsuits.

In some of the files, there was an indication that the note was made out to a particular lender and no indication that it had been transferred to MERS or at least no "chain of transfer" linking the original lender to MERS. In another files, there was in fact a lost note affidavit filed indicated another owner of the note. In some files, in the view, MERS had inconsistently listed itself as a nominee of several different owners of the note, but again showed no chain of transfer from any of them.

MERS pointed out in court that it in fact had possession of each of the notes. It took the position that it was not necessary to show a chain of title of the note from the original payee to MERS, as it was in fact only a nominee. . It acknowledged that any foreclosure proceeds would flow through MERS to the real owner of the note as shown on MERS electronic records. At one point, the court was able to get counsel for MERS to admit that MERS wasn't sure who the beneficial owner of the note was at that precise moment.

MERS nevertheless claimed that the notes had been endorsed in blank and that they essentially were bearer instruments under the UCC. Therefore, MERS physical possession of the notes should be enough to permit it to foreclose on the related mortgages, even though it acknowledged in court that it was not in fact the beneficial owner of them. There was confusing dialogue in the case, however, where the lawyers for MERS may have agreed that they didn't have the note in court and were relying upon lost note affidavits.

The court made the point that the defendants in these cases might have counterclaims against the real beneficial owners but would be barred from bringing them because they didn't know who those owners were, and furthermore they were not in court.

In the end, the court concluded that "beneficial interest to sue" cannot exist separately from other beneficial interests in the note. Since MERS claimed no other beneficial interest, its possession of the note endorsed in blank did not avail it. It commented that only positive legislation, and not contract, can establish a right to foreclose in someone other than the owner of a secured debt instrument:

> "The MERS situation seems to have resulted from the establishment of the corporation and agreements with lenders without the participation of the Florida Legislature or the Supreme Court in its rule making role. The fact that the market might find it easier to operate with the real party in interest somewhere in the background of a foreclosure lawsuit is not a compelling reason to modify the traditional requirements of a party to establish status to bring litigation."

Although the court refers to MERS as a "foreclosure agent" rather than a "servicing agent," it appears that it would also exclude servicing agents from bringing foreclosure actions.

Comment 1: The author is informed that MERS views this case as an aberration, likely resulting from the failure of local counsel to use MERS standard form pleadings, and that it anticipates that it will not have a long standing problem in Florida or anywhere else.

Comment 2: The editor is not familiar enough with MERS practices to know whether MERS typically forecloses on behalf of all registered mortgage owners or only when these mortgages are at some defined step on the way to, or after, securitization. If others know, an inquiring mind would like the answer.

Comment 3: The presence of MERS has undoubtedly led to huge savings in mortgage securitization by the "private label" process. It likely is not as critical for FNMA or FHLMC when they engage in their traditional function of acquiring loans directly from originators, but likely FNMA and FHLMC have evolved quite a lot in the current market, so MERS may play a major role in their operations as well. Whether it is necessary for MERS to perform its function for it to be involved in a foreclosure is another question. On the other hand, are there any sensible reasons why it shouldn't be able to carry out the foreclosure? The editor can't think of any, nor can he think of any reason why legislation is necessary if MERS' status as agent can be clearly made out by the contract and it produces the note.

Comment 4: It is difficult to make out all the details of the instant dispute, but it appears that in some cases there was no way to know who the true owner of the note is. This seems to be completely inconsistent with the basic notion of MERS that the owner is the party shown on MERS computer record. Consequently, it is hard to know why the owner of the note can't be named. Therefore, the problem of counterclaims that the court mentions would disappear. The mortgagee is in the suit through its agent, MERS.

MORTGAGES; FORECLOSURE; VALIDITY; BFP: Experienced investor in foreclosed properties, who purchased foreclosed property at significantly below market value, was bona fide purchaser for value. ***Melendrez v D & I Inv., Inc. 127 CA4th 1238, 26 CR3d 413 (2005)***

After the Melendrezes defaulted on their home mortgage payments and foreclosure proceedings were initiated, the Melendrezes entered into a forbearance agreement with their lender. When they missed a payment under the agreement, a trustee sale was noticed and held. The property was sold to a real estate broker, an experienced purchaser of properties at foreclosure sales, for $197,100; the fair market value of the home was between $317,000 and $380,000. The Melendrezes sued the trustee, lender, and buyer to set aside the trustee sale and cancel the trustee deed, alleging that the trustee sale was invalid for violation of the repayment agreement and the lender's internal policies. Ruling in favor of the defendants, the trial court found that the trustee sale was valid and that the buyer was a bona fide purchaser for value (BFP), and ruled in favor of the defendants.

The Melendrezes argued that under the ruling in *Estate of Yates* 25 CA4th 511, 32 CR2d 53 (1994), the buyer was not a BFP because he (1) was experienced in foreclosure sales and (2) purchased the subject property at less than market value. The court noted the conclusive presumption created by CC §2924 in favor of a BFP and the equitable rationale of protecting those who have invested value in reliance on an honest belief in the validity of the foreclosure proceedings.

The court of appeals disagreed, and affirmed. The court distinguished *Yates* as involving a faulty notice of the sale and other indicators to the buyer of irregularities in the sale, and reiterated the trial court's finding that the buyer in this matter was a BFP because he gave up something of value in exchange for the title to the Melendrezes' home and had no notice or knowledge of any defect in the proceedings. Furthermore, nothing inherently precludes an experienced foreclosure speculator who pays less than market value from being a BFP, absent a showing of fraud on the buyer's part.

Reporter's Comment 1: I can't blame Miller & Starr for asserting that "a speculator who frequently purchases at foreclosure sales who pays substantially less than the value of the property at a foreclosure sale is not a *bona fide* purchaser" (4 Miller & Starr, California Real Estate 10:210 (3d ed 2000)) based on their reading of *Estate of Yates*.. That really is what *Estate of Yates* said. I might have made a more cautious statement about it, such as "one court has characterized an experienced speculator who purchased at a foreclosure sale for substantially less than the value of the property as not a *bona fide* purchaser (BFP), and other courts may be inclined to do the same"-but I, too, read *Estate of Yates* that way.

In any event, the court was certainly not inclined to follow any such interpretation, and has made it clear that there is no blanket rule on this issue. It is now probably closer to reality to say that an experienced foreclosure buyer may or may not be treated as a BFP, depending, in part, on how much its bid was, how much of an increase over the lender's opening bid it was, and how close it came to market value-plus a lot of other things.

Reporter's Comment 2: More important, I think, is the court's holding that even if one is a BFP, the conclusive presumption of the recitals provides only limited help. Under CC §2924, the only recitals in the trustee deed that are conclusive regard mailing, publishing, and delivering copies of notices of default and sale. Although it is not uncommon (or illegal, as far as I can tell) to see trustee deeds that recite more proprieties than that, additional recitals do not come under the umbrella of statutory protection.

Some attacks on foreclosure sales may be based on improper notice, but many others are grounded in claims such as the one presented here, i.e., violation of a promise to wait longer. In those cases, it doesn't help to be a BFP rather than any other bidder (or even the lender). If the claimed irregularity is covered by a recital to the contrary, there may be a presumption against the irregularity. However, the presumption is not conclusive, and therefore probably will play no role in the litigation. If the irregularity is not within any recital, then it becomes a question of ordinary burden of proof. This is not an area where lenders, trustees, or buyers can hope to protect themselves or significantly improve their positions via better drafting. On this one, comfort can come only from the legislature.

The Reporter for this item was Professor Roger Bernhardt, of Golden Gate Law School in San Francisco, writing in the CEB California Real Property Law Reporter.

MORTGAGES; FORECLOSURE; VALIDITY; INADEQUACY OF PRICE: Alaska will set aside nonjudicial foreclosure for "grossly inadequate" price, following Restatement test.. ***Baskurt v. Beal, 101 P.3d 1041 (Alaska 2005).***

Annette Beal bought two parcels of land in 1991 for $225,000, taking subject to a blanket deed of trust in favor of the sellers on both parcels. There were two promissory notes: Note 1, for $95,000, associated with the first parcel, and Note 2, for $135,000, associated with the second parcel. Beal paid off Note 1 in 1994, but continued to make payments on Note 2 until she fell behind in 1999. The sellers' daughter, Sarah Baskurt, as trustee of their inter vivos trust, commenced foreclosure of both parcels by trustee's sale of the deed of trust.

Baskurt formed a partnership with a friend, Joyce Wainscott, and they decided to try to buy the property at the foreclosure sale. They brought cashiers' checks in the total amount of $251,000 to the sale. While waiting for the sale to begin, they encountered Allen Rosenthal, who Baskurt knew had considerable real estate experience. On the spot, Baskurt and Wainscott expanded their partnership to include Rosenthal, who had been prepared to bid up to $95,000 himself.

When biding was opened Baskurt bid $26,781.81, one dollar above the outstanding balance on the note. There were no other bids, and Baskurt, on behalf of her partnership, was declared the successful bidder.

Beal brought an action to have the sale set aside. The trial court found that the property's fair market value was the same as the 1991 selling price, or $225,000. Because the high bid at the sale was so low in comparison, the trial court set the sale aside.

The Alaska Supreme Court held that, while an inadequate price alone was not a sufficient ground to set aside a foreclosure sale, it would be grounds to do so if it was (a) "grossly inadequate" or (b) accompanied by other defects in the sale. It found both of these tests were satisfied in Baskurt, although satisfaction of either one would have warranted setting aside the sale.

On the "grossly inadequate" issue, the court quoted with approval the Restatement (Third) of Property (Mortgages) Sec. 8.3 cmt b, which adopts a figure of 20 percent of the property's market value as a rule of thumb for "gross inadequacy" of price. The bid in Baskurt, which was 11.9% of the market value, easily satisfied this test. (Inexplicably, the court refers to the bid as "less than fifteen percent" of market value; can the court really be so bad at arithmetic?)

The court also found the sale was defective because the trustee who conducted it failed to meet his fiduciary obligations – obligations that the court said were owed to both the trustor and the beneficiary. In part, these duties included taking "reasonable and appropriate steps to avoid sacrifice of the debtor's property and interest." Since the trustee conducted the sale of the two parcels in bulk when the sale of either parcel alone "would likely have generated sufficient proceeds to satisfy the amount due," the court found the sale defective. That defect, in combination with the inadequacy of the price (even if it had not been "grossly" inadequate) justified setting aside the sale.

Reporter's Comment 1: The case is significant because it clearly identifies two distinct bases for setting aside the sale: (a) gross inadequacy of price alone, and (b) inadequacy, even if not gross, accompanied by other defects – here, the trustee's sale in bulk when a sale of either parcel alone would have been sufficient. *See also Krohn v. Sweetheart Properties, Ltd.. 203* Ariz. 205, 52 P.3d 774 (2002) (employing both "gross inadequacy" and "shock the conscience" terminology in setting aside a trustee's sale for 18.07% of fair value despite absence of any other defect in the sale); *In re Edry,* 201 B.R. 604 (Bankr. D.Mass. 1996) (setting aside sale for 45.5% of fair value, where the mortgagee failed to advertise in any manner other than that required by the statute).

Comment 2: The case is one of several in recent years that imputes real duties owed by the foreclosing trustee to the trustor. Other examples include *Cox v. Helenius,* 103 Wash.2d 383, 693 P.2d 683 (1985); *Wansley v. First National Bank of Vicksburg,* 566 So.2d 1218 (Miss. 1990) (imposing a duty of commercially reasonable sale, but only for purposes of denying a deficiency judgment, not setting the sale aside); *In re Edry, supra.*

The California approach is much less pro-debtor: As the court noted in *Monterey S.P. Partnership v. W.L. Bangham, Inc*., 49 Cal.3d 454, 261 Cal.Rptr. 587, 777 P.2d 623 (1989): the similarities between a trustee of an express trust and a trustee under a deed of trust end with the name.

> "Just as a panda is not a true bear, a trustee of a deed of trust does not have a true trustee's interest in, and control over, the trust property. Nor is it bound by fiduciary duties that characterize a true trustee."

Comment 3: The court makes no reference to the fact that the mortgagee, immediately before the opening of bidding, made a deal with the only other bidder present (*Rosenthal*) to form a partnership with him, thus taking him out of the bidding. Moreover, Baskurt testified Rosenthal had been planning to bid up to $95,000 ($68,000 more than the bid entered by Baskurt on behalf of her partnership). Doesn't this constitute "chilling of bidding" by the mortgagee? Wouldn't that be an additional reason to consider the sale defective, and thus to set the sale aside even if the inadequacy of price had not been "gross?" While other bidders are certainly free to form whatever combinations they wish, doesn't the mortgagee have some obligation to avoid ruining the competitive bidding process?

The Reporter for this item was Dale Whitman of the University of Missouri School of Law, Columbia, Missouri, and the Reporter of the Restatement of Mortgages.

MORTGAGES; INSURANCE; STATUTORY REDEMPTION: When a fire causes damage to a foreclosed property during the redemption period but the deed is erroneously delivered during that time, the insurance proceeds are to be paid to the foreclosing lender to the extent of the debt and the borrower is entitled to a credit for the value of the property received in the foreclosure sale. ***Liberty Mutual Fire Insurance Company v. Alexander, 374 N.J. Super. 340, 864 A.2d 1127 (App. Div. 2005).***

A homeowner defaulted on its mortgage. The mortgagee bought the property at the resulting foreclosure sale for

$100. Apparently mortgagees had a right to seek a deficiency judgment within three months (likely subject to "fair value" limitations) but had not done so as yet.

New Jersey permits a ten day statutory redemption period following foreclosure. The foreclosing court extended this period, perhaps in connection with the mortgagor's attack on the validity of the foreclosure sale itself (which the court held to be valid.) During this extended post sale statutory redemption period, while mortgagor was still residing in the house, a fire destroyed the house. To everyone's surprise, the sheriff had inadvertently delivered the deed to the mortgagee, even though the redemption period had not run.

Later, the mortgagee sold the lot to a third party. No one at trial contested the validity of this sale, although it would appear that the mortgagor might have done so, since at the time the insurance company was aware that it had obtained the deed prematurely.

The homeowner's insurance company then filed a complaint seeking a declaratory judgment to determine how the $175,000 insurance proceeds were to be allocated. The mortgagee argued that it was entitled to the full amount of the insurance proceeds because it had obtained title to the property before the fire. The owner claimed that its right of redemption negated the erroneous transfer of title by sheriff's deed to the mortgagee and that the mortgage merged with the lien. By one construction of the mortgagor's argument, the mortgagor got to keep the insurance proceeds and the mortgagee got only the lot. The lower court held that the mortgagee was entitled to $128,081 – the amount of the unpaid debt less the amount that the mortgagee had received on the resale of the lot..

The Appellate Division affirmed the lower court's decision, holding that the mortgagee was entitled to an award of the insurance proceeds to the extent of the mortgage debt, and that the owner was entitled to a credit for the value of the damaged property that the mortgagee had obtained from a subsequent purchaser. It remanded only for purposes of determining the process amount of the debt claim that the mortgagee could make.

According to the Court, a judicial sale without an actual transfer of title is merely a contract for sale that does not extinguish the insured's interest in its homeowner's fire insurance policy. Therefore, the mortgage debt remains, and the owner is entitled to use the property to pay off the debt. In fact, it likely will be compelled to do so by the terms of the mortgage. In effect, the owner remains the title owner of the property, and in the absence of any agreement to the contrary, a mortgagee (assuming that the mortgagee is an insured under the policy, as it typically is) has the right to apply fire insurance proceeds to the outstanding debt. Unless a mortgage contains a provision to the contrary, a mortgagee cannot not be forced to convert a mortgage loan into a construction loan or to become a mortgagor's partner in rebuilding a structure. Instead, the mortgagor's debt is reduced by an amount equal to the reduction in value of the building caused by the fire so that the parties retain the same position they held prior to the fire.

Once a mortgagee acquires a property through foreclosure, it may recover, under an owner's insurance policy, for the losses incurred after it acquired title without regard to either the amount of the loan secured by the property or the amount of the debt owed by the owner at the time of acquisition.

In this case, the facts were unusual because the deed was mistakenly delivered during the redemption period, and the owner never moved to rescind the delivery. Despite that, the Court disagreed with the lower court that the result would have been the same even if the owner had been deemed to be the title owner to the property. The owner had the right of redemption at the time of the fire. The available proceeds would have been applied to the amount of the mortgage debt, in which case the owner would have been left with the land. Here, the land had been sold to a third party for its market value. Therefore the owner was put in the same position it would have been had it received the deed in exchange for extinguishment of the mortgage by payment of the insurance proceeds to the mortgagee. [Note that no one challenged the validity of the sale – as perhaps the mortgagor might have done.]

The Court rejected the owner's contention that the mortgagee had to either accept the deed to the damaged property in satisfaction of the mortgage debt and give the owner the full insurance proceeds, or accept the proceeds but return the deed. The Court's reasoning was that the mortgage debt was secured by land with an undamaged house; therefore, the mortgagee was not required to accept a deed that represented land with a destroyed house in satisfaction of the debt. Furthermore, the owner failed to explain how it would have been entitled to the insurance proceeds on land it did not own. As to the owner's alternate theory, that the mortgagee was required to accept the insurance proceeds but return the deed, the effect of the lower court's decision was that the mortgagee accepted the insurance proceeds in full satisfaction of the debt, while the owner was awarded the equivalent value of the deed as measured by the sale of the property to a third party. By crediting it with the value of the property, the lower court's decision placed the owner in the same financial position it would have been if it hadn't received the damaged property itself. For that reason, the Appellate Division affirmed the lower court's distribution of the insurance proceeds.

Comment 1: The editor has written quite a bit about the relative rights of mortgagor and mortgagee in insurance proceeds at time of foreclosure. Randolph, Patrick: "The Mortgagee's Interest in Casualty Loss Proceeds; Evolving Rules and Risks," 32 ABA Real Property, Probate & Trust Law Journal, 1 (1997) The critical issue for the editor in this case is the fact that the mortgagor was not trying to set aside the sale. If the mortgagor had set aside the sale, then in the editor's view the mortgagor certainly would have had the right to insist that the mortgagee accept the insurance proceeds in satisfaction of the debt and that the mortgagor keep the lot.

Comment 2: What the editor finds interesting in the case is the characterization of the status of the mortgagor during the statutory redemption period, in which the mortgagor is in possession of the property, as "merely a contract for sale." Certainly the mortgagor's rights to the insurance proceeds are not extinguished. But do we really have a contract of sale? Since the mortgagor can redeem, what is the sale price?

In many states, the statutory redemption price is based upon the foreclosure sale price (here $100). The editor is guessing, based upon this opinion, that redemption in New Jersey is accomplished by paying the mortgagee's total claim as approved by the court at the foreclosure sale. It was of no consequence that the mortgagee had not yet sought a deficiency, since under New Jersey procedure it still had more time to do so.

MORTGAGES; MANUFACTURED HOMES; PERFECTION: The addition of an extra bedroom on a concrete foundation and a deck did not convert a mobile home into real property, and therefore a mortgagor did not have priority as against the trustee in bankruptcy. ***In re Olson, 2005 Bankr. Lexis 1331 (Bankr. D. Kan. June 22, 2005).***

The trustee in bankruptcy sought to avoid a mortgage on the debtor's manufactured home. The mortgagor claimed that the mortgage attached because the home was set on a permanent foundation and the home had improvements built onto it. The court, applying the Kansas Manufactured Housing Act, held that to perfect a lien on a mobile home a party must note their lien on the certificate of title. The court ignored the mortgagor's argument that the dwelling was taxed as real estate. The court allowed the trustee to avoid the lien.

MORTGAGES; PREPAYMENT; PREPAYMENT PREMIUMS; YIELD MAINTENANCE: Prepayment premium provision based upon treasury yields is a reasonable attempt to liquidate damages in the event of a default and acceleration, and satisfies Bankruptcy Code test for a "reasonable charge," even when effect of application of formula is a premium of over $2 million. ***In re CP Holdings, Inc., 2005 U.S. Dist. LEXIS 24461 (W.D. Mo. 9/30/2005)***

This case involves a wretchedly written prepayment clause used in a 1989 loan. The court upheld the Bankruptcy Court's determination that the clause ought to be read to apply both to acceleration as well as other prepayment events, notwithstanding that the borrower's counsel was able to fake out the editor on the stand and interpret a segment of the note incorrectly. Other aspects of the note, and the logic of the entire arrangement, made clear that the parties' intent was to provide for a prepayment premium upon acceleration.

More interesting and valuable for posterity, however, are other aspects of the opinion, in which the court concluded that it was not unreasonable for the lender to demand a prepayment premium based upon a hypothetical yield maintenance requirement drawn from treasury yields, even though the lender, looking at the situation at the time of actual default and "prepayment," might very possibly not invest in treasuries to replace the yield, but might instead invest in higher return investments, thus profiting much more than the interest lost as a consequence of the default.

Here is the computation formula (admittedly not the greatest – but it worked):

> Said premium to be the greater of one percent (1%) of the principal amount to be prepaid or a premium which is calculated as follows:
>
> (a) Determine the "Reinvestment Yield." The Reinvestment Yield will be equal to the yield on the U.S. Treasury Issue described below ("primary issue")* published two weeks prior to the date of prepayment and converted to an equivalent monthly compounded nominal yield.
>
> (b) Calculate the "Present Value of the Mortgage." The Present Value of the Mortgage is the present value of the regularly scheduled payments to be made in accordance with the note (all regular debt service payments and/or any balloon payment) discounted at the Reinvestment Yield for the number of months remaining from the date of prepayment to loan maturity. In the event of a partial prepayment, the Present Value of the Mortgage shall be calculated in accordance with the preceding sentence multiplied by the fraction which results from dividing the amount of the prepaid proceeds by the principal balance of the loan immediately prior to prepayment.
>
> Subtract the amount of the prepaid proceeds from the Present Value of the Mortgages as of the date of prepayment. The resulting differential shall be the "Premium."
>
> As a result of there being no U.S. Treasury Issue comparable to this Note on the date hereof, the holder of this Note shall choose a comparable Treasury Bond, Note or Bill which the holder of this Note deems to be similar to the primary issue's characteristics (i.e., rate, remaining time to maturity, yield) at the time of prepayment.)

The court accepted the notion that the reasonableness of liquidated damages clauses ought to be measured on the basis of facts and circumstances existing at the time of the making of the original loan, and not "reanalyzed" at the time that default actually occurs to determine whether the parties' language remains a reasonable attempt to assess damages. This is probably the majority approach to this question, but there is some authority that would take a "second" look before approving the reasonableness of a liquidated damages provision.

The court again agreed that the use of the treasury rate is a reasonable practice for assessing the lender's probable injury, even though in virtually every case treasury yields will be lower than the yield on high grade commercial mortgages. The editor (an expert witness) testified that in general it is difficult for a lender to find comparable real estate mortgage investments that exactly match all the risk and yield characteristics of another large loan. This uncertainty is magnified when the parties were projecting in 1989 whether it would be possible, at any time over the life of the loan, to identify a comparable mortgage investment that would generate the same yield with the same risk as the original loan Thus, he testified, it was reasonable for the parties to select a stable and easily verifiable index that would move roughly in accordance with the cost of money and would certainly be a reliable computational base, even though it was not likely to correspond exactly to all the characteristics of the investment (the original mortgage) that the treasury note investment would replace.

Given the formula and the dramatic decrease in treasury yields since the making of the loan, the application of the formula in this case brought a prepayment premium of $2.6 million on a loan "prepayment" (acceleration) of $8.4 million.

It is important to note that, in this case, default and acceleration occurred prior to bankruptcy, and the court concluded therefore that Bankruptcy Code Section 506(b), which requires that fees associated with default must be "reasonable" to be permitted in bankruptcy, did not apply. Rather, the court viewed the fee from the perspective of state law on prepayment premiums as liquidated damages.

Comment: Although defeasance techniques have replaced the prepayment formula used here, the question of whether it is appropriate to use treasury yields as a computation base for otherwise uncertain yield comparisons remains an important question in many contexts, and the editor does not believe there are many published opinions validating this very common business practice. So, despite the editor's garbled language, it is possible his words, and the better stated words of Judge Fenner here, will ring through precedent.

MORTGAGES; SATISFACTION; STATUTORY PENALTIES; STATUTE OF LIMITATIONS: A claim against a mortgage arising out of a failure to timely record the satisfaction of a mortgage is a remedial action, not a penal one, and thus is subject to a six-year limitations period for actions created by a statute other than a forfeiture or penalty. ***Rosette v. Countrywide Home Loans, Inc., 825 N.E.2d 599 (Ohio Sup. Ct. 2005).***

Mortgagors sought statutory damages, costs, and interest from Mortgagees under Ohio statute R.C. 5301.36©) which provides damages of $250 for failure to timely record mortgage satisfactions and releases. The statute requires that such recording must occur within 90 days of the payoff. In each case, the trial court denied certification to the proposed out-of state class and certified the Ohio mortgagor class, but only those cases meeting the one-year statute of limitations in R.C. 2305.07 applying "for a penalty or forfeiture."

Mortgagors appealed, arguing that R.C. 5301.36©) is remedial rather than penal, and that therefore a six-year statute of limitations should apply under R.C. 2305.07. The appellate court affirmed the trial courts' rulings for the one-year limitation and additionally ruled that Mortgagors' appellate notice of appeal had divested the trial courts of the ability to modify their class certification, thus rendering the appeal itself moot.

Mortgagors appealed both findings to the Ohio Supreme Court. The court reviewed the statute to determine the legislative intent underlying it. The court found that since the statute used the word "damages", the legislature must not have meant a penalty or a forfeiture, citing other Ohio statutes, such as R.C. 1321.56, which do explicitly identify financial payments as penalties or forfeits. Since the $250 payment is not a penalty or forfeiture, it falls within the provision in R.C. 2305.7 for actions other than penalties or forfeitures, which carries a six-year statute of limitations. The appeals court erred in upholding the trial courts' application of the one-year limitation and in finding the appeal moot. The court case remanded the case to the trial court for further proceedings.

Comment 1: Six years is a long time for a nice fat class to develop. The mortgagees will be required to provide to the plaintiffs their own records, which should make shopping for the late settlements relatively painless at $250 a pop. Note, however, that other jurisdictions have penalties (damages???) far greater than this.

Borrowers, of course, rarely suffer more than inconvenience (which can be substantial) when lenders are sloppy about releasing. Title companies in many areas of the country insure over a late delivered satisfaction. But there are risks, of course, and in any event prompt satisfaction is part of what the borrower bought when it took out the mortgage. The mortgagee accepted the interest and fees, didn't it? And it's not too patient with borrowers who aren't punctilious about their payments.

Comment 2: Lenders concerned about the penalties associated with late releases ought to take a look at the new Uniform Mortgage Satisfaction Act, released last year by NCCUSL. Although it doesn't solve all problems, the Act attempts to balance the interests of lenders and borrowers and focuses much more on getting the title cleared than it does on nicking careless mortgagees in massive class actions.

MORTGAGES; SECURITIZATION; MERS: Florida trial court rules that MERS lacks status to foreclose as representative of lender even when MERS holds the note. ***In re Mortgage Electronic Registrations Systems, Inc., Cir. Ct. Pinellas County, Fla., Walt Logan, Judge, 8/18/05) (Numerous case numbers)***, discussed under the heading: "Mortgages; Foreclosure; Procedure; Standing to Foreclose."

MORTGAGES; STATUTORY REDEMPTION; INSURANCE:: When a fire causes damage to a foreclosed property during the redemption period but the deed is erroneously delivered during that time, the insurance proceeds are to be paid to the foreclosing lender to the extent of the debt and the borrower is entitled to a credit for the value of the property received in the foreclosure sale. ***Liberty Mutual Fire Insurance Company v. Alexander, 374 N.J. Super. 340, 864 A.2d 1127 (App. Div. 2005)***, set forth in under the heading: "Mortgages; Insurance; Statutory Redemption."

MUNICIPAL LAW; IMMUNITY; ANNEXATION;: City officials cannot be held liable for antitrust violations when acting in their official capacity. ***GF Gaming Corporation v. City of Black Hawk, 405 F.3d 876 (10th Cir. 2005).***

Business and property owners from Central City, Colorado, sued city officials, casinos, and private parties in the neighboring town of Blackhawk, based on alleged violations of antitrust laws. Central City and Blackhawk are both mountain towns that allow gambling. When the plaintiffs filed suit, the main access to Central City passed directly through Blackhawk. Plaintiffs claimed that city officials in Blackhawk conspired to prevent Central City from annexing property to create a road directly to Central City, bypassing Blackhawk, and that Blackhawk officials attempted to divert customers from Central City by engineering road construction and detours in Blackhawk.

A Colorado statute requires 50% of landowners within the area of the proposed annexation to vote in favor of annexation. Black Hawk officials allegedly conspired with private persons to buy four mining claims within the area of the proposed annexation. Black Hawk then sold undivided one percent interests in the mining claims to 14 individuals and business entities for $500 each. The plaintiffs alleged the sole purpose of these conveyances was to cause the percentage of landowners approving the annexation to drop below the required 50%. After the Federal District Court for Colorado dismissed plaintiffs' claims, they appealed to the Tenth Circuit.

The Tenth Circuit affirmed dismissal of plaintiffs claims. The court first dismissed plaintiffs claim for declaratory or injunctive relief as moot, finding that a highway had been built at a different location. The court also found the Blackhawk city officials to be immune from monetary liability under the Sherman Act, reasoning that, although their motive in selling the mining claims might have been unlawful, the city officials acted within the scope of their official duties.

OPTIONS; RIGHT OF REFUSAL; ENFORCEABILITY: A right of first refusal is not enforceable due to vagueness where it does not contain a price term and does not specifically state that price will be set by a competing offer. ***Crestview Builders, Inc. v. The Noggle Family Limited Partnership, 816 N.E. 2d 1132 (Ill. App. 2004).***

Plaintiff Crestview entered into a real estate sales contract with defendants, the Noggle Family Limited Partnership, pursuant to which plaintiff purchased from defendant several tracts of land and defendants agreed to provide plaintiff with "a right of first refusal on the retained homestead." There was apparently no dispute as to what parcel was intended by the term "retained homestead."

The parties were unable to negotiate mutually acceptable terms for the right of first refusal, and in the interim defendants conveyed the homestead parcel to two of the partners in their individual capacities. Three years after this conveyance, the parties inserted language at the bottom of a closing statement for the sale of another parcel that stated that defendants would comply with the terms of the original purchase agreement and deliver a signed and recordable right of first refusal by the end of the year. Defendants failed to do so, and plaintiff brought suit for declaratory judgment and specific performance.

The circuit court granted plaintiff's summary judgment motion, and defendants appealed, arguing that the right of first refusal provision was unenforceable due to the lack of a price term. Citing *Universal Scrap Metals, Inc. v. J. Sandman & Sons, Inc.,* 786 N.E.2d 574 (2003), the court observed that a right of first refusal need not provide a price term if it provides a mechanism whereby price may be ascertained. Plaintiff contended that the term itself contained an implicit mechanism for determining price, citing Black's Law Dictionary for the proposition that a right of first refusal is defined as the right to meet the terms of a third party's offer if the seller intends to accept that offer. But the court rejected plaintiff's contention, finding that a right of first refusal need not always involve a third party offer (citing the *Universal Scrap Metal* case for authority.)

The court noted that other jurisdictions have agreed that a right of first refusal ought to be construed as requiring the holder to match the terms of a competing offer, but indicated that Illinois had reached a different conclusion. It stated that sometimes parties intend that the property be offered first to the holder of the right as a precondition to even offering the property for sale to anyone else. Where the terms of the agreement do not indicate whether the parties intend this type of right of first refusal, as opposed to the "match the offer" type, the court will hold the entire right unenforceable for vagueness.

Comment 1: In the editor's experience, at least, the term "right of first refusal" has a reasonable well established trade meaning that ought to be enforced when the parties have not indicated otherwise. That meaning is the "match a competing offer" type of right. It bothers the editor that the court does not come up with a "default construction" for the right of first refusal – finding it to be a "match the competing offer" type of arrangement, rather than a "first offer" arrangement and put the burden on the party benefitting from an alternative interpretation to make that idea clear. There is no question in most of these cases, especially when other land is transferred, that the right of refusal is a valuable item for which the parties paid a price. Why should the court read the whole thing out of the contract and give the seller a free ride?

Comment 2: It may be that courts see this as one of those "story" situations – based upon some myth, usually involving a "landed poor" saintly farm family getting snookered by sharpy developers. Courts that suck into these kind of storybook interpretations of legal principles often tend to tilt the law away from a need for clarity and in favor of protecting parties that they perceive to be in need of greater protection, whether or not they make any real investigation as to the accuracy of the assumption or the appropriateness of the remedy.

NATIVE AMERICAN LANDS; INDIAN LAND CONSOLIDATION ACT; BUREAU OF INDIAN AFFAIRS; CONVEYANCE: A member of a recognized Indian tribe may convey an interest in restricted land to the tribe by gift despite the Bureau of Indian Affairs' concerns about fractionation of tribal restricted land. ***Miami Tribe of Oklahoma v. United States, 374 F. Supp. 2d 934 (D. Kan. 2005).***

A member of the Miami tribe wanted to convey 1/3 of his 3/38 restricted undivided interest in 35 acres to the Miami tribe by gift. The Bureau of Indian Affairs denied the tribe member's application to gift the land. The Bureau decided that even though the tribe member had a special relationship with the tribe, no special circumstances justified allowing the gift and that the conveyance would further fraction individually owned Indian lands. The Bureau applied two regulations in its decision. The first, 25 C.F.R. § 152.23, outlines the procedure for conveying restricted Indian lands, and the second, 24 C.F.R. § 152.25(d), outlines the standard for allowing conveyances for less than market value or no consideration. Section 152.25(d) allows conveyances for less than market value if the grantee of a conveyance is in a "special relationship" with the grantor and there are special circumstances. Based on these statutes, the Bureau held that it was against the Bureau's policy to allow conveyances for less than market value, and that the conveyance would not help consolidate ownership of the land into a usable parcel.

The Miami tribe intervened, and sought review of the administrative decision. The court, after examining the statutes, expressed disbelief at the Bureau's reasoning and found no grounds for the Bureau's stated policy of not allowing less than market transfers when the transfer is between an individual and their tribe. As to the Bureau's argument that it would further fraction the land; the court accepted the tribe's argument that it would actually serve to consolidate ownership of the land in the long term. Based on these reasons, the court overturned the Bureau's decision.

OPTIONS; RIGHT OF FIRST REFUSAL; CONDITIONS: A landlord may not defeat a tenant's right of first refusal to purchase real property by tying the sale of that property to another property, and the tenant may not obtain specific performance as to both properties. ***397 West 12th Street Corp. v. Zupa, 799 N. Y. S.2d 192 (A.D. 1 Dept. 2005).*** The plaintiff was a tenant in premises owned by the defendant and held a right of first refusal to purchase the property. The defendant entered into a contract of sale for the property occupied by the plaintiff and entered into a second contract to sell another property he owned. Both the defendant and the prospective purchaser agreed that the two contracts would close simultaneously or neither would close. The plaintiff alleged that the price of its property was increased above market value and that the price of the second property was decreased below market value in an attempt to circumvent the right of first refusal. The plaintiff was seeking to compel the sale of both properties to itself or, alternatively, to reduce the price of its property to fair market value. The court held that although the plaintiff cannot enforce specific performance for both properties, the defendant may not defeat the plaintiff's right of first refusal by tying the two properties together.

OPTIONS; TYING ARRANGEMENTS: A servitude requiring a subdivision lot purchaser to give a builder an option to purchase the property for the original purchase price if the purchaser does not contract with the builder to build on the property within four years is not an unreasonable restraint on alienation or an unlawful tie in. ***Vande Guchte v. Kort, 13 Neb. App. 875, 2005 Neb. App. Lexis 214 (9/6/05) ;(related unpublished opinion at 2005 Neb. App. Lexis 206 No. A-03-1345 (9/6/05)***

Builder entered into an agreement with a subdivision developer to provide "consultation, suggestions and recommendations" regarding the development of, and final plat for" a residential development of golf course lots. In consideration for these services, the developer appointed Builder the "exclusive builder" of homes on lots sold by developer within two years of the issuance of the final plat and on all townhome lots sold within seven years. To implement this concept, the developer gave to Builder a nonexclusive option to purchase any lot in the development for the initial price per lot as shown on an attached price sheet.

The parties later modified and extended the Builder's rights and established a required contract provision in the sale of every lot that created a binding servitude on each lot sold that gave to Builder an exclusive option to purchase the bound lot for the price paid by the original purchaser from the developer in the event that the lot purchaser failed to enter into a contract with Builder to build on the property within four years of purchaser's closing on the acquisition of the lot. The option gave Builder one year to exercise the option following the expiration of the four year period for contracting.

Vande Guchte purchased one of the lots for $145,000 and did not enter into a contract with the Builder during the four year period. Midway through the fourth year following his closing, Vande Guchte contracted to sell the lot to a third party for $179,000, but the sale fell through when the title company noted the option to purchase held by the builder and purchaser's lender refused to loan. Subsequently, the builder tendered to Vande Guchte a contract to purchase the property for $145,000 and Vande Guchte responded with a lawsuit seeking a declaration that the option was void and unenforceable and claiming that Builder had intentionally interfered with Vande Guchte's contract to sell the property at a favorable price to the third party. Builder answered and sought specific performance of its tendered purchase agreement. Vande Guchte also sued his buyer for specific performance.

The trial court found for Builder on Vande Guchte's complaint and granted Builder specific performance. In a separate opinion, it concluded that Vande Guchte's had no obligation to perform because the option restriction rendered the title unmarketable and because the financing contingency had not been satisfied.

On appeal: *Held:* Affirmed (both cases). The Builder's option did not constitute an unreasonable restraint on alienation nor an unlawful tying agreement and specific performance was appropriate.

The specific performance case, which is the only published decision, is particularly noteworthy because the court points out that a higher standard of equity is necessary to support such a remedy. Here there was no question of lack of clarity in the agreement nor of notice to Vande Guchte. The sole question was whether the agreement violated some public policy.

The court held first that there was no unlawful restraint on alienation. Noting that most servitudes and public land use restrictions make property more difficult to sell, the court concluded that the mere fact that Vande Guchte could not sell for his optimal price did not render the Builder's restriction an unenforceable restraint on alienation. The restraint was not a direct prohibition on resale, it noted, because during the four year period prior to the option kicking in, Vande Guchte was free to sell to anyone he wished (subject to the servitude.) After the option kicked in, Vande Guchte was restrained, but only for one year. The court didn't even mention this one year restraint, but clearly the relatively short period was of no concern to it.

As to the argument that there was an unlawful tying arrangement, the court agreed, as Builder conceded, that this agreement clearly tied the sale of the property to the Builder's construction services. But not all tying agreements are unlawful. There must also be"sufficient economic power on the part of the defendant in the tying market to appreciably restrain competition in the tied product market, combined with the exercise of such power to coerce the purchaser to buy both items. Further, the amounted of commerce affected must not be insubstantial. The court commented that these are both the common law (Restatement) standards and the federal antitrust standards.

The court concluded that Vande Guchte had produced not evidence that the developer that sold the lot to Vande Guchte occupied a dominant position in the relevant market – in fact Vande Guchte didn't even provide evidence of what the relevant market was. It commented that the "uniqueness" of land by itself does not establish economic power.

Comment 1: Note that, although in the published opinion the court concludes that Vande Guchte was not restrained unreasonably from selling the property subject to the servitude, it also upheld the trial court's finding that the servitude rendered his title unmarketable.

Comment 2: Note also that there is not one word about privity of estate or touch and concern the land requirements, both of which arguably were not satisfied here, as the builder had no interest in the subdivision land or other benefitted land at the time of the original agreements. . Perhaps the reason is that this agreement was structured as an option – the conditional transfer of an interest in land to Builder – rather than a restrictive servitude.

Comment 3: In the current hot market, many builders and other service providers are attempting to create tie in arrangements. The Builder had some good lawyers in the development of the scheme here. The way in which the Builder's benefit was established gave the Builder a nice fat time within which to bargain with the lot owners but did not tie up the land for so long as to offend the sensibilities of the court. The use of the option price, rather than some more draconian form of enforcement mechanism, also softened the impact of the restraint. Others would do well to study the device used here to see whether their clients can accept this device as their tying method.

Comment 4: Nebraska has always been somewhat conservative (and, in the editor's view) correct, in its analysis of the restraint on alienation issue. In the case cited as support for its conclusion here, *Occidental Sav. & Loan Assoc. v. Venco Partnership,* 293 N.W. 2d 843 (1980), the court resoundingly rejected the argument that the due on sale clause was a restraint on the alienation of property, thus rejecting the *Wellenkamp* decision in California and leading other courts away from the error of the California decision (which later was mooted by the Garn-St. Germain Act.) It is an interesting footnote to history that the seminal law review article that *Wellenkamp* relied upon when it kicked off the "due on sale" fracas was written by a law professor at the Creighton University in Omaha, Nebraska, Ron Vollkmer.

Comment 5: Vande Guchte attempted to raise on appeal the argument that the servitude was unlawful because it called for a penalty, but the court refused to consider that argument as it had not been raised below. It is difficult to tell whether the court was exercising commendable restraint in reviewing the case and simply ignored the issue, or whether it might be avoiding deliberately a question it deemed to be more problematic. From the editor's standpoint, an option to purchase always has an element of penalty when it calls for sale of the property at a price lower than current market, but that is the nature of the parties' agreement, and if the optionee is ready willing and able to perform, as here, it is difficult to view the consequence to the optionor as a penalty.

Here, of course, there's another twist – the option is a response to the lot purchaser's failure to enter into a contract to build with Builder. But note that the lot purchaser has no duty to enter into such a contract – there is merely an option to work with this Builder or else sell back to Builder. If the court did not find this arrangement violative of public policy on the grounds raised in the suit, it is difficult to conclude that the court would recharacterize the arrangement as a contractual obligation to deal with the Builder backed by a penalty option.

RECORDING ACTS; NOTICE; CONSTRUCTIVE NOTICE; INDEXING: Pennsylvania Supreme court rules that "index is not part of the record" in Pennsylvania. Misindexed mortgages still provide constructive notice. ***First Citizen's Nat'l Bank v. Sherwood, 879 A.2d 178 (Pa. 2005)***

This case resolves, presumable permanently, the construction of the present Pennsylvania scheme of recording laws. The court holds that a mortgagee provides constructive notice by properly delivering a proper document for recording, and the fact that the Recorder's office later misindexes the mortgage, so that it can't be found by subsequent title searchers, does not affect the priority of the first mortgage against subsequent purchasers.

This decision places Pennsylvania with the majority of jurisdictions that interpret their own recording acts to provide that the "index is not part of the record." There is a substantial and respectable minority, however, and many scholars are of the view that making the index part of the record is the best result from a policy standpoint. They argue that, as between two innocent parties, the party that ought to bear the consequence of the potential error by the recorder's office is the one in a position to cure that error. A mortgagee that records its mortgage can later return to the recorder's office to check the index and, if necessary, to request its correction, in order to be sure that there is proper constructive notice of its claim. A subsequent purchaser has no ability to correct that which, to it, is as a practical matter undiscoverable. Therefore, scholars argue, the burden ought to be on the recording mortgagee, and the way to accomplish this is to rule that a mortgage is not constructive notice if not discoverable in the index.

The court does not pick sides in this policy debate, at least not openly. It purports simply to interpret the Pennsylvania statute, 21 P.S. Sec. 357, to provide that recording is not necessary. It states simply that when a written instrument relating to real property is recorded, the effect is to give constructive notice to subsequent parties.

The opposing interests, and two judges in dissent, argued that this statute is superceded in application by a more specific statute, 16 P.S. 9853, which states that when a written instrument is indexed, such indexing will be notice to all parties of the recording itself. The proponents of the "index" view argued that the obvious obverse of this precept is that unindexed instruments to not provide constructive notice. The dissenting judges noted that this statute appears in a chapter denominated "mortgages" in the statute book, while Sec. 357 appears in a chapter denominated "deeds and conveyances." The dissent further argued that chapter 357, because of the location in the conveyancing chapter, applies only to permanent interest in real property. The majority responded that indeed a mortgage in Pennsylvania is permanent, because Pennsylvania has adopted the "title theory" of mortgages, giving the mortgagee good title to the property itself when the mortgage arises. Thus, the mortgage should be evaluated by the conveyancing statute's terms, and in any event Section 357 is much newer and therefore supercedes Section 9853 to the extent that they are in conflict.

Comment 1: Certainly this case is not about statutory interpretation. The court could easily have interpreted the statutes to require proper indexing. The majority attempts to reconcile the two chapters before it concludes that one superceded the other. In fact, they could peacefully coexist if the dissenters' view was adopted.

This has got to be about policy – and the concern that to make the index part of the record would render all title plants in limbo for a longer period of time as the documents are recorded and then delivered out to the title plants. The title companies are likely to be the ones who would have been condemned to this limbo, as they'd be expected to insure good title to the property and bear the risk of unrecorded mortgages later popping up. Unlike ownership or leasehold estates, mortgage holders do not take possession, so there is no opportunity to learn of them except through recording.

Comment 2: The more important aspect of this case is that it reverses, and thus removes from precedent, the absolutely horrible lower court decision, reported as the DIRT DD for 6/30/03. The decision held that whether or not an misindexed deed ought to provide constructive notice depended upon whether it reasonably could be found through a search of an electronic index – leading to courts to decide on a case by case basis whether a reasonable search was possible. The injury done to predictability of title was patent in this case, and the editor tap danced all over it. He is happy to see this decision chase the earlier *Sherwood* case into oblivion.

Comment 3: Note that the case also eradicates the danger to attorneys who fail to follow up to be sure that indexing did occur, as happened to the Pennsylvania attorney in Antonis v. Liberati, the DIRT DD for 6/18/03, a case whose precedential significance now also vanishes. . All DD's can be found on the DIRT website http://www.umkc.edu/dirt.

Comment 4: Although stated as an opinion of the Pennsylvania Supreme Court, the heading indicates that the opinion is by the "Middle District" of that court, so perhaps this is a small panel, and there may be a further appeal.

RESTRAINTS ON ALIENATION; CONDOMINIUMS; USE RESTRICTIONS; SALE OF UNITS: Condominium association, through amendment of bylaws, can restrict sale of small studio apartments in complex of much larger apartments so that studios can be sold only to owners of one of the larger apartments. ***Demchick v. 90 East End Ave. Condominium, 796 NYS2d 72 (App. Div. 2005)***, discussed under the heading: "Condominiums; Use Restrictions; Sale of Units."

SERVITUDES; RESTRICTIVE COVENANTS: Restrictive covenant requiring that a building "be kept in good repair" does not prevent burdened party from replacing historic elements of property with replicas.. ***Town of Butternuts v. National Grange, 773 N.Y.S.2d 775 (A.D. 3 Dept. 2005).***

In 1952, the Town of Butternuts conveyed title to the former village hall to the defendant Grange subject to the conditions that the Grange (I) keep the building in good repair, (ii) maintain the hall for public use and (iii) permit the Town to use the property for elections and the like. In an effort to raise money for necessary building repairs, the Grange attempted to sell the historic weathervane atop the building, replacing it with a replica and the Town objected.

In finding for the defendant, the Court held that the law favors free and unencumbered use of real property, and covenants restricting use are strictly construed against those seeking to enforce them. In light of that policy, the Court held that there was no covenant restricting the sale of the weathervane.

The Town maintained that extrinsic evidence would show that it was the intent of the parties that the actual antique elements of the building be preserved. The court responded that this is not what the contract said, and that extrinsic evidence cannot be introduced to modify the meaning of unambiguous language.

Comment: Note that in a few jurisdictions (the editor seems to recall that New Mexico is one), the ordinary rule that extrinsic evidence of intent is admissible only in the event of ambiguity has been abandoned. The court will always entertain evidence as to the true intent of the parties. What a bad idea for real estate deals, where typically both sides think about what they are saying and ought to be bound by what they conclude.

SERVITUDES; TYING ARRANGEMENTS: A servitude requiring a subdivision lot purchaser to give a builder an option to purchase the property for the original purchase price if the purchaser does not contract with the builder to build on the property within four years is not an unreasonable restraint on alienation or an unlawful tie in. ***Vande Guchte v. Kort, 13 Neb. App. 875, 2005 Neb. App. Lexis 214 (9/6/05) ;(related unpublished opinion at 2005 Neb. App. Lexis 206 No. A-03- 1345 (9/6/05)***, discussed under the heading: “Options; Tying Arrangements.”

SUBDIVISIONS; TYING ARRANGEMENTS: A servitude requiring a subdivision lot purchaser to give a builder an option to purchase the property for the original purchase price if the purchaser does not contract with the builder to build on the property within four years is not an unreasonable restraint on alienation or an unlawful tie in. ***Vande Guchte v. Kort, 13 Neb. App. 875, 2005 Neb. App. Lexis 214 (9/6/05) ;(related unpublished opinion at 2005 Neb. App. Lexis 206 No. A-03- 1345 (9/6/05)***, discussed under the heading: “Options; Tying Arrangements.”

VENDOR/PURCHASER; BUYER’S PERFORMANCE: A purchaser’s delay in extinguishing a seller’s mortgage debt is not a material breach of a sales contract and does not warrant recession. ***Singh v. Carrington, 796 N.Y.S.2d 668 (A.D. 2 Dept. 2005).*** The purchaser of real property had to extinguish the existing debt of the seller in order to comply with the terms of the sale contract. The purchaser could not extinguish the debt prior to the closing date and the seller sued the purchaser for delay of performance, requesting that the contract of sale be rescinded. The Court held that delay in performance of a contract where time is not of the essence is not ground for rescission and directed the seller to execute the deed transferring the property to the purchaser.

VENDOR/PURCHASER; BUYER’S REMEDIES; SPECIFIC PERFORMANCE: : Buyer’s inability to tender the purchase price or a signed mortgage agreement rendered the meant that they could not succeed in an action for specific performance. ***Thomas v. Laustrup, 800 N.Y.S.2d 238 (A.D. 3 Dept. 2005).*** The plaintiffs contracted to purchase a motel from the defendants. Because one of the defendants had advanced dementia and Alzheimer’s disease, her husband signed on her behalf pursuant to a power of attorney. Shortly thereafter, the defendant attempted to cancel the contract and claimed that because certain key terms were not included in the contract, it had no legal effect. Alternatively, the defendants claimed that the power of attorney was ineffective due to lack of capacity. The court found that the uncertified and unsworn medical records concerning capacity were insufficient to support a summary judgment finding in favor of the defendants. However, the court refused to grant specific performance for the plaintiffs because they failed to demonstrate that they were “ready, willing and able to perform on the original closing date.”

VENDOR/PURCHASER; DISCLOSURE; STATUTORY REQUIREMENT: Exclusion of condominiums and cooperatives from the definition of “residential real property” in the property disclosure statutes violates the Equal Protection Clause. ***Goldman v. Fay, 797 N.Y.S.2d 731 (N.Y.City Civ.Ct. 2005).***

The purchaser of a condominium discovered faulty air conditioning pipes and sued the seller of the property, stating that seller knew of the condition when it sold the condominium to purchaser. The property disclosure statutes of New York require that a Property Condition Disclosure form be completed prior to entering into a contract for the sale of residential real property. The law, however, explicitly excludes the sale of condominiums and cooperatives from the definition of "residential real property".

The court stated that the exclusion of condominiums and cooperatives from the definition of residential real property violates the Equal Protection Clause of the U.S. Constitution. It called upon the New York legislature "to either repeal the current law or stay its execution until the defects can be remedied [by adding a disclosure requirement for condominiums and cooperatives.]

The court acknowledged that one reason for the distinction might be that the information concerning the character of the property called for in the report might be less available to sellers of condominium or cooperative apartments than they would be to owners of free standing homes, because repair and maintenance of an apartment unit typically is the responsibility of an association or manager, and not the owner of the unit. . The judge characterized this argument as a "red herring," at least with respect to the unit itself, as opposed to the common areas. The judge took the view that the burden of filling out the form would not be onerous, and would provide valuable information to the buyer.

The court acknowledged that there was no statutory disclosure required here, so the common law rule requiring disclosure of known latent defects applied. The court concluded that the purchaser was not entitled to damages because it could not prove that the seller had actual or constructive knowledge of the faulty air conditioning pipes. Even if the purchaser could prove that the seller had knowledge, the purchaser could not recover the expenses of repairing the faulty air conditioning since the repairs were done by an unlicensed home improvement contractor.

Comment 1: This is just a trial court opinion, apparently, but it is rather extreme in its position, so the editor thought it worth noting. It is unlikely to be appealed because the court found as a matter of fact that there was no liability for nondisclosure.

Comment 2: It strikes the editor as rather bizarre that there would be no "rational basis" for a statute that imposes disclosure responsibilities on owners of free standing houses but not on owners of cooperatives or condominiums. And certainly there are not such protected interests at stake here that any more rigorous test would apply. It's a provocative thought, though.

Comment 3: Much of the required information on the New York form strikes the editor as requiring quite a bit of inquiry on the part of an apartment dweller, and in fact disclosure would require more effort and uncertainty than would be the case with a homeowner. The editor doesn't see what the big deal is. But the editor is no judge, and therefore doesn't get to sprinkle his writing, as the court did here, to quotes from "Little Orphan Annie" and "The King and I."

VENDOR/PURCHASER; EARNEST MONEY; LIQUIDATED DAMAGE PROVISION: A liquidated damages provision of a purchase agreement limiting damages to earnest money does not preclude Plaintiff's recovery of monthly rent when Defendant retains possession of the property under a rental arrangement as a tenant pending completion of the sale and not as Buyer. ***Khatib v. Bolton, 618 S.E.2d 9 (Ga. App., May 5, 2005).***

Seller agreed to let Buyer take possession of subject property prior to closing date in exchange for monthly rental fee. After the closing fell through, Seller brought action against Buyer to recover rent for over six months. The trial court entered judgment in favor of Seller and Buyer appealed.

Buyer had signed a purchase and sale agreement containing a liquidated damages provision. Buyer argued that the liquidated damages provision in the purchase agreement precludes the Seller's recovery of the monthly rent and limits damages to the earnest money.

The Court of Appeals found that although the purchase agreement provided that Seller was entitled to retain the earnest money as liquidated damages in the event of Buyer's breach, the Court also found that since Buyer was allowed possession of the premises, Buyer was obligated to pay rent to Seller until the time of closing. Even though the closing did not occur, Buyer was responsible for paying rent as long as he remained in possession of the premises as his possession was under the rental arrangement as a tenant pending completion of the sale, and not as a Buyer.

Comment: Why bother to appeal? The amount of the forfeiture was $50,000 and the judgment for rent and late fees was likely another $50,000. That smarts!! The Seller's counsel got very lucky here. Logically, it certainly makes sense to view the rental agreement as a separate item, but the rental agreement was in "special stipulations added to the agreement.." In other words, it was part of the agreement, and the agreement provided that the deposit was forfeited as liquidated damages (presumably) for breach of the agreement. Whoops!! Logic and sense prevailed, but don't try this at home, kids.

VENDOR/PURCHASER; INSTALLMENT LAND CONTRACTS; INSURANCE; PROCEEDS: Purchaser under installment contract is entitled to entire proceeds of insurance policy carried by vendor, even though proceeds exceed balance owing on the contract. ***Estes v. Thurman, 2005 WL 2046008 (Ky.Ct.App. Aug. 26, 2005).***

Thurman entered into an installment contract sale of a house to Estes for $17,000. (Sounds as though the "housing bubble" hadn't hit that part of Kentucky.) The contract, which called for payments over a seven-year period, included a covenant by the purchaser to carry casualty insurance. The purchaser took possession and began making payments, but did not buy insurance. Instead the vendor, Thurman, carried insurance on the property. There is no clear explanation in the opinion as to why the insurance was purchased and paid for by the vendor rather than the purchaser.

Six months later the house burned down through no fault of either party. The balance owing on the contract was about $16,000 at that time, but the insurance company paid Thurman $34,000. Thurman, the vendor, then filed a suit to forfeit the purchaser's rights under the contract on account of the purchaser's default in failing to carry insurance. The purchaser filed a counterclaim for (1) a deed to the property (on the ground that the insurance proceeds had paid off their contract balance in full, and (2) the remaining $18,000 in insurance proceeds!

The court found for the purchasers! It held that the insurance proceeds were held by the vendor in a "constructive trust" for the benefit of the purchasers. It would be unjust, the court held, for the vendor to benefit from the insurance by more than the value of the vendor's security interest, which was $16,000. So the purchasers got the rest of the money.

Reporter's Comment 1: There is nothing unusual about a court giving a purchaser credit, as against the purchase price, for the insurance proceeds collected by the vendor on the vendor's insurance policy. Numerous cases uphold this principle, although they sometimes deduct from the credit the amount of the premiums that the vendor paid (on the ground that if the purchaser is going to benefit from the insurance, the purchaser at least ought to pay the cost of it). *See, e.g., New Hampshire Ins. Co. v. Vetter,* 326 N.W.2d 723 (S.D.1982); *Fellmer v. Gruber*, 261 N.W.2d 173 (Iowa 1978); *Chapline v. North American Acceptance Corp.*, 25 Ariz.App. 465, 544 P.2d 682 (1976). A court that refused to grant this sort of credit would put the vendor in the position of being able to both (1) collect on the insurance, and (2) collect the full remaining purchase price from the purchaser – a pretty clear case of unjust enrichment of the vendor.

Reporter's Comment 2: In the present case, however, the court goes far beyond merely giving the purchaser a credit to avoid unjust enrichment of the vendor. Here the purchasers not only got their land paid for, but (if the $17,000 price they agreed to was equivalent of fair market value) also got another $17,000 as a pure windfall. And they got it as a result of an insurance policy they had no part in obtaining or paying for, and despite the fact that they breached the contract by failing to obtain their own insurance – an act that surely would have been wise, as well as being a contractual duty. The vendor, on the other hand, had his contract paid off, but nothing further to show for the insurance he paid for.

Reporter's Comment 3: It appears that there is inevitably a windfall for someone here, since the insurance company seems to have paid out about twice what the property was worth. Shouldn't that windfall go to the party who had the gumption to buy the insurance?

Editor's Comment 1: Let us assume that there had been no fire, but the seller acquired the insurance. Would the seller have been able to charge the buyer for the insurance as damages for the buyer's nonperformance of the contract? The answer, of course, is "yes." In fact, the typical contract provides that the party to be benefitted by the insurance may buy the insurance and collect the cost as part of the next installment, backed up by whatever remedies exist for default of an installment.

I would assume that if the seller were buying insurance on the buyer's account as described above, the seller would be obligated to treat the insurance as the buyer's insurance, and itself as a "mere trustee" of the proceeds to the extent they exceeded the protection of the seller's security interest

Thus, the editor is bemused, but not shocked, at the result here.

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Editor's Comment 2: The above certainly would be true in a mortgage, where the mortgagee's sole interest is in being paid. Is it any different in an installment land contract, where the seller is still technically the legal owner of the property and has a potential right to forfeit the contract? Maybe.

VENDOR/PURCHASER; INSTALLMENT LAND CONTRACT; SELLER'S REMEDIES: Where an installment land contract is breached, but there is no provision providing for forfeiture of monies paid, seller may terminate the contract only through rescission, which requires refund of all monies paid by buyer. Even if there is a forfeiture provision, it is subject to liquidated damages analysis in Georgia. ***Crowell v. Williams, 273 Ga.App. 676, 615 S.E.2d 797 (2005).***

The Court of Appeals held that a party may rescind a contract without the consent of the other party on the grounds of nonperformance, only when both parties can be restored to the condition in which they were before the contract was made.

The Court relied on underlying premise that the partial payment of the purchase price gave the Plaintiff an equitable interest in the land to the extent of his investment. In as much as Georgia law abhors forfeitures, absence of a written contractual provision specifying a forfeiture in the event of nonpayment requires that the partial payment be returned to the Plaintiff. Even if there is a contractual provision that specified forfeiture, such would constitute a liquidated damages provisions and would only be enforced in certain situations. No such evidence is present in this case.

Defendant continued to hold possession and title to the land and offered it for sale to another, thus showing he had elected to rescind the contract with Plaintiff. When a contract is rescinded, the parties are not to be left where the rescission finds them. The original status must be restored, an equivalent therefore must be provided in the contract or furnished by the law. Accordingly, the Court of Appeals held that Defendant should restore the Plaintiff's money paid and reversed the judgment of the trial court and remanded the case for judgment to be entered in favor of the Plaintiff.

VENDOR/PURCHASER; MISREPRESENTATION; FRAUD; "AS IS" CLAUSE: A claim by purchasers who bought home "as is" and sued for damages based on mold in the property may survive the defendant seller's motion to dismiss, even though the purchasers had signed a mold waiver, where the seller knew and failed to disclose that the property had leaks needing repair**.** ***Larson v. Safeguard Properties, Inc., 2005 U.S. Dist. Lexis 15333 (D. Kan. July 13, 2005).***

Purchasers signed a contract to purchase on May 4, 2004. On the same day, they also signed addendums affirming that: 1) they purchased the property "as is" without warranties by the seller; 2) they should use due diligence to discover mold on the property; and 3) they agreed to release seller and its agents from any liability that resulted from mold.

Prior to closing on June 1, 2004, subcontractors of a cleaning company hired by the informed the seller that there was a significant leak in the basement that needed to be fixed. Seller did not reveal the leak, and closed the transaction. Subsequently, purchasers sued based on allegations that mold made the house uninhabitable. The court held that the deciding factor in the case was whether the purchasers could have discovered the defect through a reasonable inspection. Because the reasonableness of the inspection created a question of fact, the court refused to grant the seller's motion to dismiss.

The sellers argued, of course, that the specific language of the "mold waiver" should have put the buyers on notice to make a more thorough inspection for mold. Obviously, it was found later (probably by a very intrusive inspection, as one of the buyers fell ill, allegedly from mold allergy.) But the court said that the fact that the buyers were informed of the possible presence of mold does not preclude the question of whether the mold was reasonably discoverable, although it might be some evidence as to what would have constituted a reasonable inspection.

Comment 1: The upshot of this case appears to be that even an express buyer's waiver against an identified risk will not insulate the seller from failure to disclose a latent defect. There is at least a small argument that the court would have considered enforcing the "as is" clause if the failure to disclose had been negligent (as the facts in this case finally may show) and there was a specific release of negligence claims as part of the "as is" clause. But it is hard to parse the court's opinion in such a way to conclude that a deliberate disclosure or nondisclosure can ever be avoided by an "as is" clause where the defect could not be discovered by reasonable inspection.

Comment 2: Some jurisdictions take the position that fraud is never avoided by an "as is" clause. Clearly Kansas – the law applied here – does not take that position. See *Alires v. McGhehee*, 85 P.3d 1191 (Ka. 2004) (the DIRT DD for 4/5/04). (Buyer made no inspection whatever). A recent Texas case held that the an "as is" clause will not protect the seller against fraud where the fraud itself misled the buyer into underinspecting or not inspecting. *See Savage v. Doyle*, 2004 Westlaw 2964634 (Tex. App. 12/16/04) (The DIRT DD for 2/14/05). Another case worth looking at is *Syvrud v. Today Real Estatae, Inc*., 858 So. 2d 1125 (Fla. App. 2003), also a water leakage case with an "as is" clause, where the court held that the "as is" clause did not excuse the broker's nondisclosure – period – unless it specifically stated that the broker was excused from failure to disclose relevant facts. This was the DIRT DD for 8/9/04) All the DD's can be found on the DIRT website – http://www.umkc.edu/dirt

VENDOR/PURCHASER; MISREPRESENTATION; HOME CLEANING AGENCIES: Home repair contractor retained by seller to fix up house prior to sale has no duty to notify buyers of known latent defects discovered during the process of repair. ***Larson v. Safeguard Properties, Inc., 2005 U.S. Dist. Lexis 15333 (D. Kan. July 13, 2005).***

The contractor hired a carpet cleaning company, which in fact discovered the leaking conditions. The court held that the carpet cleaning subcontractor was an agent of the contractor and that any knowledge it obtained was imputed to the company, and would have support a claim for fraudulent nondisclosure had there been a duty to disclose.

Further, the court held that the absence of any privity of contract with the buyers did not necessarily preclude a claim for fraud against the contractor. It noted that a duty to disclose can arise outside of a contract relationship. But it noted that the plaintiff buyers here had not alleged any other circumstances that would impose such a duty on the contractor, and in fact had not opposed its summary judgment motion at all. So the contractor walks. (The seller – to whom the carpet cleaner has given actual notice of the leak – were not so lucky.)

Comment: The editor doesn't quarrel with the result, but is a bit concerned about the *dicta* suggesting that if a carpet cleaner hired by the contractor discovers a defect, and fails to inform the seller, the contractor could be liable for fraudulent nondisclosure because the carpet cleaner was the contractor's agent. Could this rule also be extended to a situation where a seller hires a home cleaning expert and the expert discovers defects and fails to inform the seller? Is the seller still liable for failure to disclose known defects when it has only constructive, and not actual knowledge? Is it liable for fraud? Let's hope this language by the court was just a little loose jaw flapping, since it was simply *dicta.*

VENDOR/PURCHASER; MISREPRESENTATION; STATUTE OF LIMITATIONS: Statute of limitations will bar home buyers from suing broker or seller for negligent misrepresentation when they were shown and purchased a house that the seller did not own, rather than house across the street that it did own, where they moved into the house they thought they had bought and lived there for more than five years before the real owner of their house knocked on their door. But buyers parallel fraud action may proceed if they reasonably relied upon fraudulent statements and reasonably did not discover they had been defrauded until within the two year limitations period on such actions. ***Gilmore v. M&B Realty Co., 895 So. 2d 200 (Ala. 2004)***

First time homebuyers contacted a broker to buy a home. They were shown a house by a broker that the broker believed was listed with the brokerage office by the Veteran's Administration. Not surprisingly, the broker's recollection was vague as to just what happened, but he showed the homebuyers the vacant house across the street instead. The broker claimed that, for this to have happened, there had to be a working lockbox on the house and paperwork to sign inside regarding the listing.

Part of the confusion stemmed from the fact that the VA, in dealing with the house, consistently used the address "4369 Bayou Drive." In fact, the house address of the VA-owned home was 4360 Bayou Drive, and the house across the street was 4361 Bayou Drive. 4361 was owned by a builder, who apparently was paying very little attention to it. The 4369 address was a vacant lot.

Homebuyers alleged that the broker told them that the house had a new roof and had recently been painted. And, of course, the broker told them that the house was for sale, listed by the VA.

The homebuyers decided to buy the house, signing a contract listing the property as "4369 Bayou Drive." The took a mortgage from the VA and the VA got a lender's policy. The legal description contained a subdivision lot designation for what was really 4360 Bayou Drive, but no one knew it. Homebuyers moved into what was really 4361 Bayou Drive and lived there relatively uneventfully for 6 years, making some improvements and paying annual taxes (presumably on 4360 Bayou Drive.) The tax bill came to their house, although they listed the address with the tax collector as 4369 Bayou Drive. Apparently the tax collector credited the payments on 4360 Bayou Drive. They did not get an owner's policy of title insurance, but it is unclear that would have made much difference here.

Everyone was aware that the address on the front of the house was not 4369, but they assumed that this was as VA error in the designation of the house located at 4361, and, assuming that the red tape would grow waste high if they tried to change things, they designated the property as 4369 on all VA documents. One tax document that one of the buyers signed did show the correct address, but only in the corner with a lot of other technical numbers, and she missed it. The court said that this was a reasonable "miss."

More than five years after homebuyers moved into their little nest, the developer who really owned the house showed up. They sued the VA, the brokerage, and the sale agent, for wanton negligence and fraud.

The trial court granted summary judgment for defendants on the negligence and fraud claims, based upon the running of the two year statute of limitations on negligence. The court held that no real damage need be suffered as a consequence of negligence to trigger the running of the statute of limitations. All that has to happen is that the act of negligence be completed. Ignorance of the tort or injury are irrelevant if there is no fraudulent concealment by defendants.

The Alabama Supreme Court here affirmed the dismissal of the negligence claims. But it reversed the trial court (by a split decision) on the fraud allegations. The Alabama statute in this case is also two years, but does not begin to run until "the discovery by the aggrieved party of the fact constituting the fraud."

The defendants argued, of course, that the homebuyers had not relied reasonably on any alleged fraud, since there was the mention of the correct address in one of the documents and parties are expected to read the documents. But the court noted that the fact of the true address was not prominent in the documents. A reasonable person, exercising ordinary care, might have missed them, or at least the likelihood of such is sufficient to survive summary judgment. The court also stated that other circumstances wouldn't have led homebuyers to discover the fraud. It cited as evidence supporting this claim that the broker didn't find the problem. [But note, for these purposes, we would be assume that the broker was being fraudulent – so the broker in fact would have known of the problem under that assumption.]

The court held that even though the contract stated that buyers could conduct an independent title search, it did not require them to do so, or to buy their own title insurance.

Comment: Now what happens? We go to the jury on the argument that the broker (and possibly the VA) fraudulently sold the wrong house to the buyers. To what end? They couldn't have anticipated that fraud of this nature wouldn't be exposed within the two year period, and there would have been hell to pay. There simply was not motive for fraud here. It was just bonehead stupidity, perhaps driven by the obstinacy of the VA bureaucracy in other instances that led everyone to pussyfoot around the problem.

But we're going to an Alabama jury with innocent young homebuyer plaintiffs who have lost their home. So expect a settlement.

Comment 2: By the way, the roof was not new and the house had not been painted. This was true both of 4360 and 4361. So there will be fraud damages here if the buyers can convince the court that the broker told them this. Once again, normally no big deal, but here the defendants will want to settle to avoid the floodgates from opening.

VENDOR AND PURCHASER; PROCEDURE; *RES JUDICATA:* . Lease/Purchaser's claim for, *inter alia*, breach of land sales contract was barred by *res judicata* as a compulsory counterclaim that ought to have been filed in response to vendor's earlier forcible entry and detainer action brought in capacity as landlord. ***Forney v. Climbing Higher Enterprises, 815 N.E.2d 722 (Ohio App. 2004).***
Plaintiff tenant/purchaser filed suit in November 2002 against defendants sellers for breach of contract, fraud, negligence, and violations of the Consumer Sales Practices Act. In 1998, plaintiff had entered into a land sales contract with sellers, one of the terms of which required sellers to obtain insurance coverage on the property. Sellers neither obtained coverage nor disclosed to plaintiff the lot's propensity to flood, and in 1999 the lot flooded, causing the alleged injury and loss to the plaintiff.

In their answer to plaintiff's claim, defendants pleaded *res judicata* and collateral estoppel as an affirmative defense, and subsequently moved for summary judgment. In 2000, defendant Climbing Higher had filed claims against plaintiff for eviction and money damages; the magistrate allowed the writ of eviction and later entered a default judgment on the claim for money damages.

The trial court in the instant case found that plaintiff's claims here were compulsory counterclaims that should have been filed in response to defendant Climbing Higher's earlier cause of action. Citing *Haney v. Roberts,* 720 N.E.2d 101 (1998), the appellate court observed that in an action for forcible entry and detainer, if the landlord does not join any other action, the tenant need not file counterclaims. It pointed out that a forcible entry and detainer action involves relatively informal procedure and does not involve a jury. It would be inappropriate to compel a tenant to bring a counterclaim in such an action if it chooses not to do so. If, however, if the landlord does join another action with the forcible detainer and entry action, then the summary nature of the proceeding is abrogated and Civ.R. 13(A) will apply to compel counterclaims in appropriate cases.

(The court expressly excluded from its analysis the special situation of defenses raised for breach of the implied warranty of habitability.)

Here, because the defendant's earlier action as landlord did join a claim for money damages, Civ.R. 13(A) applies, and the court moved to a consideration of whether it the compulsory counterclaim rules ought to apply to tenant's action. The court followed the two-part test set forth in *Rettig Enterprises v. Koehler,* 626 N.E.2d 99 (1994), which states that a party invoking a bar based upon a compulsory counterclaim must show that (1) the claim existed at the time of the first pleading and (2) the claim arose out of the transaction that is the subject matter of the opposing claim. The appellate court found that because the flooding occurred a year before landlord/vendor's claim was filed, all of appellant's claims existed at that time, and because the claim arose out of the land sales contract and the subject matter of that contract (the property) the basis for each cause of action was the same.

The court further concluded that, although the forcible entry and detainer action was brought by only one of the defendants, that defendant was in privity with the other defendants in plaintiff's instant suit, and thus all were protected by the compulsory counterclaim rule.

Comment 1: According to UMKC's civil procedure maven, David Achtenberg, this case is mainstream on the procedural issue. David notes that some statutes do provide for a claim for "rent and possession," in which a counterclaim might not be available (and thus would not preclude a subsequent claim by the tenant/defendant). But if the counterclaim was available — both in the sense that it existed and in the sense that it could be asserted in the landlord's proceeding — David thinks modern courts would pretty uniformly agree with the Ohio court.

Comment 2: There's a useful object lesson here. Even if your tenant client is disgusted with the whole affair and is willing to depart from the premises, a summary possession action is nothing to take lightly – be sure to inquiry carefully as to other damages claims that the tenant might want to press. It's not uncommon for a landlord to add a claim for rent damages as well as possession, and that's all it took in this case to trigger the compulsory counterclaim rule.

VENDOR/PURCHASER; STATUTE OF FRAUDS; RATIFICATION: Despite fact that real estate agent forged sellers' names on sale agreement and related documents, where buyers in fact negotiated the contract and verbally agreed to it, and later executed escrow and disclosure documents in preparation for sale, sellers ratified the contract notwithstanding lack of their signature and buyers may sue for specific performance. ***Behniwal v. Mix, 2005 Westlaw 2404612 (Cal. App. 9/30/05)***

Buyers submitted an offer to purchase condominium home, and sellers responded with a multiple counteroffer, inviting buyers to respond to a proposed increase in price. This counteroffer was sent to several prospective buyers, with full disclosure that this was happening. Because the counteroffer was sent to several people, it provided that it would not be effective unless and until sellers signed the accepted counteroffer. Buyers executed and delivered the counteroffer to Sellers' broker. It was undisputed that the broker then forged the signatures of the Sellers to the counteroffer document. Sellers denied that they knew of this forgery, but the trial court did not believe them.

Subsequently, an escrow "was opened," likely by the Sellers' broker, and Sellers executed certain documents routinely required at the early stages of escrow, including a disclosure with respect to registered sex offenders, which referenced the sale agreement documents and stated that it was incorporated into that agreement. The signatures of Sellers on this document was noticeably different from those on the sale agreement, but Buyers had no actual knowledge of the forgery and apparently didn't notice the difference.

Later, one of the Sellers sent a handwritten note to escrow requesting an extension of the closing by thirty days. Thereafter, one of the Sellers took ill, and he escrow was postponed for six months, and one of the Sellers again delivered to her broker a handwritten consent to the extension. A month after that, however, both Sellers sent a handwritten note delivered to escrow asking that escrow be cancelled for health reasons.

The appeals court appears somewhat dubious of the health claim, as the evidence showed that the Sellers had received and treated as a "back up" an offer to purchase their condo for $20,000 more than the $540,000 price agreed to in their deal with Sellers, but the trial court bought the illness explanation, and the appeals court saw no need to specifically challenge it in light of the appeals court's ruling.

The trial court had refused to grant specific performance, due to the failure of the contract to satisfy the Statute of Frauds, but awarded attorney's fees to the Buyers anyway, payable by the broker, whose forgery led to this mess. In fact the court ruled that Sellers could recover attorney's fees, nominally against Buyers, but also payable by the broker. The fees appear to have been substantial – a total in excess of $169,000 prior to the costs of the appeal. Buyers and broker crossappealed, and the appeals court reversed both rulings. It held that Buyers could proceed with specific performance because Sellers had ratified the contract by executing various documents through the early course of the closing purporting to advance the closing, knowing that the Buyers believed that they had executed the contract. The court reversed the attorney's fee ruling against the broker, but remanded for a determination as to whether the Buyers, now prevailing parties, were entitled to attorney's fees from the Sellers.

The court took care to indicate that its finding was that the Sellers had ratified the contract, and was not based upon an estoppel theory, which Buyers had not plead. The court held that the agent's signature for the Sellers on the original counteroffer document constituted their formal acceptance of the counteroffer. Although they had not authorized the broker in writing to act as their agent for these purposes, the court held that Sellers' execution the very next day of the various disclosure documents, all referencing the sale agreement, established that they had ratified the broker's behavior.

It was important to the court that it draw a distinction between alleged ratification of the contract itself by the execution of the disclosure papers, which it specifically did not find had happened, and ratification of the agent's execution of the original contract, which thus bound the Sellers – which the court did find had occurred.

In an important additional piece of analysis, the court held that the Buyers here did not need to show that they still had a committed loan in order to satisfy the requirement that they were "ready willing and able" to buy – a common requirement in specific performance actions. Buyers only had to show that they had the wherewithal to secure a necessary loan within a reasonable period of time. The Buyers had blown virtually their entire earnest money deposit on attorney's fees, the had arranged for a personal loan from a relative to cover that amount, and the court noted that the attorney's fee award in the outcome of the case likely would solve that problem anyway.

Comment 1: The case is nicely written and thoughtfully presented. It shows some sympathy for the Sellers, who were in their 70's and dealing with illness, but indicates that the trial court had made extensive efforts and mediation which had failed. Some of that failure must be laid at Sellers' feet (or their counsel.)

Comment 2: The court also comments in a footnote that an estoppel theory might also have worked, but it's nice to have a clear ruling on the ratification issue. The court pointed out that the disclosure documents were not themselves escrow papers incorporating the entire deal, but only referred to the deal, but under the circumstances were adequate to establish ratification.

VENDOR/PURCHASER; RELIGIOUS INSTITUTIONS: A religious corporation may not be awarded specific performance of a contract for the purchase of real property without first complying with relevant religious and not-for-profit corporation law. ***Scher v. Yeshivath Makowa Corp.*, 799 N.Y.S.2d 106 (A.D. 2 Dept. 2005).** The plaintiff sued for specific performance or damages arising out of the defendant religious corporation's failure to complete the sale of real property. The lower court awarded specific performance of the contract at a price of $218,000. On appeal, however, the Court reversed and held that the lower court erred in rewriting the contract insofar as it changed the agreed-upon price. Furthermore, the Court held that no court can award specific performance to a religious corporation without first determining whether the proposed sale of real estate complies with religious and not-for-profit laws governing the sale of real property by such a corporation.

VENDOR/PURCHASER; TYING ARRANGEMENTS: A servitude requiring a subdivision lot purchaser to give a builder an option to purchase the property for the original purchase price if the purchaser does not contract with the builder to build on the property within four years is not an unreasonable restraint on alienation or an unlawful tie in. ***Vande Guchte v. Kort, 13 Neb. App. 875, 2005 Neb. App. Lexis 214 (9/6/05) ;(related unpublished opinion at 2005 Neb. App. Lexis 206 No. A-03-1345 (9/6/05)***, discussed under the heading: "Options; Tying Arrangements."

WORDS AND PHRASES; "BUILDING:" Each townhouse in a complex of townhouses is a separate building for the purposes of exemption from the provisions of the Chicago Residential Landlords and Tenants Ordinance. ***Allen v. Lin, 826 N.E.2d 1064 (Ill. App. Ct. 2005)*** discussed under the heading: "Landlord/tenant; Residential; Warranty of Habitability."
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WORDS AND PHRASES: "PERSON:" In context of an insurance policy providing coverage for wrongful eviction a "person" wrongfully evicted must be a human being, and not a business. ***Mirpad v. California Insurance Guarantee Assoc., 34 Cal. Rptr. 3d 136 (Cal. App. 9/19/05)***, discussed under the heading: "Insurance; Definitions; "Person:"

ZONING AND LAND USE; CONSTITUTIONAL LAW; TAKINGS; REGULATORY TAKINGS; PROCEDURE: A mandamus claim based on an alleged regulatory taking cannot be said to be "unripe" where the city denies a building permit in order to obtain a public benefit. ***Duncan v. City of Mentor City Council, 826 N.E.2d 832 (Ohio 2005).***

Duncan purchased a parcel in the Shiloh Park Subdivision that contained a creek to which the City of Mentor, Ohio ("Mentor") had easement rights. Duncan applied to the Municipal Planning Commission of Mentor to build a single-family residence on his parcel. The planning commission determined that the subdivision's declaration of covenants, conditions and restrictions had designated Duncan's parcel a common area and not a buildable lot and denied Duncan's application.

Duncan filed a complaint for a writ of mandamus to compel appropriation proceedings to determine compensation for the city's taking. The Court of Appeals, Lake County, determined that Duncan's mandamus claim was not yet ripe because the planning commission's denial of Duncan's application did not constitute a final determination concerning the application of regulations to the property since the decision was based on the private restrictive covenants of the subdivision declaration rather than on the application of any Mentor zoning ordinance. Thus, the court of appeals entered summary judgment in favor of the city.

The Supreme Court of Ohio reversed. Summary judgment is appropriate if there is no genuine issue of material fact, the moving party is entitled to judgment as a matter of law and it appears from the evidence that reasonable minds can come to but one conclusion, and construing the evidence most strongly in favor of the nonmoving party, that conclusion is adverse to the party against whom the motion for summary judgment is made.

Contrary to the court of appeals' argument, the planning commission had reached its final decision when it denied Duncan's application.

ZONING AND LAND USE; ENVIRONMENTAL IMPACTS; SHOPPING CENTERS: California courts wrestle with question of environmental impact of supercenter. ***Maintain Our Desert Environment v. Town of Apple Valley, 124 Cal. App. 4th 430, 15 Cal. Rptr. 3d 322 (2004); Bakersfield Citizens for Local Control v. City of Bakersfield, 22 Cal. Rptr. 3d 203 (Cal. App. 2004)***, discussed under the heading: "Environmental Law; Environmental Impact; Retail Development."

ZONING AND LAND USE; ESTOPPEL: City will be estopped from reneging on building permit after applicant has invested substantially in project, even when permit issued erroneously and in violation of settlement agreement that applicant previously had entered into with City. ***Congregation Etz Chaim v. City of Los Angeles, 371 F. 3d 1122 (9th Cir. 2004)***

The Congregation owned property in a residential neighborhood that had used as a location for its religious practices, in violation of local zoning ordinances, for 18 months. Other residents of the neighborhood objected. There was litigation in state and federal court, including a claim under the Religious Land Use and Institutionalized Persons Act. On the eve of the hearing on this Act, the parties reached a settlement agreement by which the Congregation agreed to "the single family character of the property shall be restored and maintained, including the residential character and architecture" the action was dismissed, with the Federal District Court retaining jurisdiction over the carrying out of the dispute. The Agreement obviously contemplated that new permit applications might be made by the Congregation in "restoring" the property, and required submission of plans for approval within 90 days. It provided expressly that the "any notice, tender or delivery or other communication pursuant to the Settlement Agreement" would be submitted by the Congregation was to a specified individual in the City's large planning department who lots of experience on this dispute and the neighborhood. This person was vested with responsibility by the City to monitor compliance with the Agreement.

Instead, the Congregation ignored the specified individual and submitted building plans to other persons in the City building department and obtained a building permit. The plans called for expansion of the existing home from 3145 square feet to 8150 square feet, an expansion guaranteed to infuriate the neighbors and, in the view of the City, wholly inconsistent with the Agreement. It did submit a copy of the Agreement along with the plans, and negotiated for three months both with the building department and a City Attorney lawyer who also had a copy of the Agreement, paying over $20,000 in permit fees.

Upon receiving the permit, the Congregation immediately commenced with its "remodeling." The first step consisted of utterly demolishing the existing house, leaving only two exterior walls standing. The neighbors immediately ran to Mr. Green, who apparently learned for the first time of the "end run." He concluded that the Agreement did not contemplate a massive expansion of the size of the house as a "restoration."

When the City tried to stop work and suspend the permit, the Congregation returned to Court and got an injunction against the City action based upon estoppel. The Ninth Circuit Court of Appeals, upheld the estoppel claim by a split decision, including a clear and sensible dissent.

The court held that California had a well established doctrine of estoppel, and that this was a relatively clear case, as there had been extensive negotiation with the City, which had then issued a permit, resulting in reliance by the Congregation that now appeared to be irreparable. It noted that whether the Congregations activities in fact were inconsistent with the Agreement was a "nice question," but not one that it needed to consider, as the City was estopped from raising it.

Of course, the City responded that the Congregation had violated the Agreement by failing to notify Mr. Green, and that it therefore had "unclean hands" and should not benefit from the estoppel. The Court responded that the submission of plans in connection with a permit application was not clearly a "notice, tender, delivery or other communication . . . .” as contemplated by the agreement to be addressed to Mr. Green.

Comment 1: Give us a break!!! As the dissent points out, this isn’t even a close case. The Agreement specifically contemplated that there would be construction and that the plans would be submitted to the City, so how could the subsequent permit application not be a “communication” under the Agreement? The parties had selected Mr. Green, out of over 47,000 employees of the City, to receive this communication. To anyone looking on from the outside, there does seem to be some bad faith going on.

Comment 2: On the other hand, there had to be some very bad lawyering going on as well, since the lawyer for the City Attorney’s office who had a copy of this Agreement also did not communicate with Mr. Green. Perhaps the lawyer believed that Green had received notice from the Congregation, but verification of this fact was only a phone call away. Is it possible that the Congregation selected people in the Planning Office who might have been favorably disposed towards its case? The Editor has no inside information on this point, but is struggling to understand how a case of this evident notoriety within the Planning Department sat there for three months without Mr. Green’s notice, especially when the Agreement contemplated the submission of new plans within 90 days to restore the property.

Comment 3: Don’t try this at home, kids. Zoning estoppel may be common in California, as asserted by the court, but in fact there is a long tradition in most jurisdictions of protecting the body public from carelessness by its own employees, and other jurisdictions might have had no problem in letting the City dodge this bullet.

ZONING AND LAND USE; PRE-EXISTING NONCONFORMING USES: Notwithstanding issuance of a building permit and certificate of occupancy, if landowner’s use of property for s truck maintenance business is carried out without a special use permit in violation of a zoning bylaw, it does not attain lawful nonconforming status, and a separate statute of limitations barring actions to terminate uses already commenced by landowner and its tenants does not make future uses through additional tenants valid as nonconforming uses. ***Bruno v. Board of Appeals of Wrentham, 818 N.E.2d 199 (Mass. App. Ct. 2004)***.

In 1984, Delphic obtained site plan approval from the Wrentham Planning Board to operate a truck maintenance and refueling depot on its land. In 1985, the Wrentham building inspector issued a building permit to Delphic, and a certificate of occupancy was issued later that year. At the time Delphic received this site plan approval and these permits, the Wrentham zoning bylaw (“Bylaw”) required such a use to not only obtain site plan approval, but also a special permit from the Board. Delphic did not obtain any special permit at that time.

In March 1996, Delphic’s was considering bringing a new tenant onto the property, perhaps in conjunction with existing tenants. That tenant applied for an occupancy permit, and the building inspector denied that request on the grounds that the special permit requirement of the Bylaw had not been complied with. The Wrentham Zoning Board of Appeals (“ZBA”) upheld the building inspector’s determination, and Delphic appealed. A Superior Court judge found that because the use of the property for truck maintenance was not lawful when it began in 1985, the use was not permitted to have protection under G.L. c. 40A, §6 as a prior nonconforming use. The Appeals Court agreed.

In its argument to the Appeals Court Delphic asserted that the Board’s 1984 site plan approval was the functional equivalent of a grant of a special permit; and that the unlawful use of the facility without a special permit, but with an original issued building permit, acquired lawful nonconforming status under G.L. c. 40A, §6, once the statutorily prescribed six-year time limitation has passed. The court rejected all three arguments.

The Court also rejected Delphic’s contention that the Planning Board’s approval of the site plan application was the functional equivalent to a grant of a special permit. Delphic claimed that under the 1984 version of the Bylaw, the site plan and special permit standards for approval were “virtually identical” and that the Board’s approval of the site plan was equivalent to a special permit because the Board made an “undisclosed or unexpressed determination that…the proposed use complied with the bylaw.” The Court disagreed, noting that special permit review is a statutorily created process, whereas site plan approval is a process established by a municipality. Wrentham “clearly differentiates” between the two, placing them in different articles of the Bylaw. Further, here the Board’s decision granting site plan approval applied conditions only applicable under the site plan article, and did not recite any of the standards applicable to special permits.

Lastly, the Court denied the portion of Delphic's appeal that claimed that the use at the property had acquired legal nonconforming status. G.L. c. 40A, §7 states that "if real property has been improved in accordance with the terms of the original building permit," no action to declare that use violative of zoning, or otherwise unlawful, shall be permitted unless it is brought within six years of the commencement of the alleged violation. G.L. c. 40A, §6 states that a bylaw "shall not apply to structures or uses lawfully in existence or lawfully begun…before the first publication of notice of the public hearing on such…bylaw."
Delphic argued that because the use of the facility for truck maintenance was begun under an "original building permit," the fact that no one challenged the use for six years allowed the use to garner lawful, but nonconforming status. The court reiterated that the running of the limitations period in §7 does not render the structure or use lawful, but rather merely immunizes it from an enforcement action. The court also ruled that the limitation period in §7 only applies to initially lawful uses. Not only does §6 expressly not refer to §7, to extend its protection here would "impermissibly augment the extent" of the relief afforded by §6 by allowing unlawful uses to attain zoning protection. For these reasons, the court held that Delphic's unlawful use was not converted to a lawful nonconforming use under §6.

Comment: This case is a lot closer than might first appear. The editor is not sure that the statute of limitations of Section7, above, is all that common, and it adds an interesting twist here. Delphic and its prior tenants, apparently, will be permitted to continue the activities they began under the original building permit, even though they are characterized as "unlawful." But Delphic will not be able to rent to additional tenants. (The court noted that in a footnote that it did not have before it the question of whether the bar of Section 7 extends to benefit "successors in interest" of Delphic, but doesn't really say how the instant case is different.)

The court also admitted that *dicta* in prior cases did contain language suggesting that an activity protected by the statute of limitations was the equivalent of a nonconforming use and ought to be analyzed the same way.

We really don't know, at least from this opinion, what subtle differences there are between Delphic operating a truck maintenance facility with existing tenants and operating with new tenants. The difference is only technical, it would appear, but technical means a lot in the zoning world.

ZONING AND LAND USE; RELIGIOUS PRACTICES: Religious Land Use and Institutionalized Persons Act protects requires "least burdensome alternative" approach to achieving public land use goals that substantially interfere with sincere religious practices, even if those practices are not "fundamental" to religious beliefs. ***Grace United Methodist Church v. City of Cheyenne, 2005 WL 2746701 (10/25/05)***

Church sought a variance to open an expanded day care center (75 students) in the Church facility. The applicable zoning ordinance permitted day care facilities of no more than 12 children. The city refused the variance. The Church argued that its day care center was a religious activity entitled to protection under various elements of the United States Constitution and the relatively recent Religious Land Use and Institutionalized Persons Act. The city noted that the facility would admit children who were not affiliated with the Church and teachers also were not required to be associated with the Church.

The Church challenged the City's action in federal court, and the trial court affirmed, following a jury trial on the RLUIPA claim as to whether the Church's day care activities were based upon a sincerely held religious belief.
On appeal, the court had little problem in this case batting down the Constitutional arguments. It concluded that there was a neutral compelling state interest in enforcing zoning rules of the sort here, and that the burden religious practices was insubstantial, as the Church could open a day care center at another, lawful, location. The only discussion of note in this part of the case was the discussion of whether the existence of certain other available exceptions to the zoning requirements triggered special Constitutional scrutiny when the city refused to grant an exception to the Church. The ordinance permitted exceptions for "churches," "schools" and "other uses similar to those permitted in this district." The Church argued that the zoning ordinance therefore was not one of "general application," and that the City's refusal not to provide an exception for the Church constituted discrimination.

The court agreed that there was a doctrine permitting challenge to apparent "general application" policies when adopted exceptions permitted government to make special exceptions. It said, however, that there was not general agreement as to what number or nature of exceptions would trigger this doctrine, which it termed the "individualize exception" doctrine. And the few exceptions permitted in this ordinance did not, in court the court's view, justify the conclusion that the policies behind the ordinance were not of "general application." It concluded that there was no *per se* rule that the existence of any exception will put into question the neutral purpose of a public ordinance.

> As the district court correctly observed, several "federal courts have held that land use regulations, i.e., zoning ordinances, are neutral and generally applicable notwithstanding that they may have individualized procedures for obtaining special use permits or variances." Indeed, in the land use context, the Sixth, Seventh, Eighth, and Eleventh Circuits have rejected a per se approach and instead apply a fact-specific inquiry to determine whether the regulation at issue was motivated by discriminatory animus, or whether the facts support an argument that the challenged rule is applied in a discriminatory fashion that disadvantages religious groups or organizations."

The court concluded that a regulation that contains broad, objective exceptions does not set up a subjective system of individualized exceptions that triggers heightened scrutiny. This approach has been applied in the past even when zoning laws have been applied to prohibit the location of a Church building itself in contravention of zoning rules.

Of more interest in the decision was the court's analysis of the federal statute specially protecting religious practices from zoning regulation beyond Constitutional minimum standards. RLUIPA sets up a strict scrutiny standard for the implementation of land use regulations. In essence, a land use regulation cannot "substantially burden" "religious exercise" unless the government can show the regulation furthers a compelling governmental interest and is the least restrictive means of furthering that interest.

The court instructed the jury, *inter alia,* that for protected religious exercise to enjoy protection under RLUIPA the activity must constitute "conduct or expression that manifests some tenet of the institution's belief" and curtails its "ability to express adherence to its faith," or denies it "reasonable opportunities to engage in those activities that are fundamental to the institution's religion." The church objected to the instruction and asked the court to substitute the word "important" for "fundamental." The court refused.

On appeal, the church contended that the instruction overstated its burden because RLUIPA does not require the religious activity that is substantially burdened by the land use regulation at issue to be "fundamental." The 10th Circuit Court of Appeals agreed. Although the requirement that a protectable religious belief had to be "fundamental" might have been the standard under prior law, the court concluded that the recent enactment of RLUIPA modified the requirement.

> "In ruling [in a prior case] that the pastoral visits requested by [a] prisoner were protected activities under RFRA, we stated:
>
> > 'The term "exercise of religion" was previously defined in RFRA as "the exercise of religion under the First Amendment to the Constitution." See 42 U.S.C. 2000bb-2(4) (1999). RLUIPA amended RFRA, however, so that "exercise of religion" now means "religious exercise, as defined in [42 U.S.C.] 2000cc-5." Id. 2000bb-2(4). "[R]eligious exercise" is defined in 42 U.S.C. 2000cc-5(7)(A) to include "any exercise of religion, whether or not compelled by, or central to, a system of religious belief." Plaintiff does not claim the requested pastoral visits were required by his religious beliefs. Under the definition of "religious exercise" in 42 U.S.C. 2000cc-5(7)(A), however, a religious exercise need not be mandatory for it to be protected under RFRA. . . . .
> >
> > In other words, whatever the substantial burden test required prior to the passage of RLUIPA, the statute substantially modified and relaxed the definition of "religious exercise."

Consequently, the challenged instruction was improper. Although other instructions were deemed to be more proper, the court agreed that this instruction might have misled jurors, but it nevertheless refused to reverse the trial court decision because the jury made a specific finding that the Church's conduct was not based upon a "sincerely held religious belief," and consequently the fact that the belief in question was fundamental or not was not at the root of the trial court decision.

An interesting, and ironic, feature of the case was that the trial court evidence included a letter from the local Methodist bishop to the Church's pastor, in which he initially refused to provide financial support to assist the Church in its litigation over the day care center. The letter stated that the bishop viewed the day care proposal as a "secular" proposal and not entitled to support from the larger church resources. The bishop later changed his views, helped to finance the litigation, and explained his change of heart in court. But the letter, admitted as an admission, may have influenced the jury.

Comment 1: The case is a good source of case analysis on a number of church vs. zoning authorities issues. But of greatest interest to the Editor is the notion that if a religious organization does maintain a sincerely held belief that proposed conduct is based upon its religious views, it won't matter that the proposed activity is not central to the liturgy or core beliefs of the organization. Sooner or later this will make a difference in a religious practices zoning dispute.

Comment 2: It's not clear to the editor, however, that if the Church had established that it's conduct was entitled to protection under RLUIPA. It still would have had to demonstrate that there was a "substantial" impact on its religious practices in order for the city to demonstrate that there was no reasonable alternative in achieving its zoning goals other than to prohibit that conduct. Close call. Does the day care center have to be at the Church to achieve its religious goals? Are economics to be taken into account (probably not – the editor guesses.)

ZONING AND LAND USE; RESTRICTIVE COVENANTS: Where City refuses building permit and decision is based upon restrictions contained in private covenants, and such covenants were part of subdivision documents that the City reviewed in connection with subdivision approval, City's decision is an application of public policy and can be regarded as a regulatory taking.

***Duncan v. City of Mentor City Council, 826 N.E.2d 832 (Ohio 2005)*,** discussed further under the heading: "Constitutional Law; Takings; Regulatory Takings; Procedure."

The Court of Appeals, Lake County, determined that Duncan's mandamus claim was not yet ripe because the planning commission's denial of Duncan's application did not constitute a final determination concerning the application of regulations to the property since the decision was based on the private restrictive covenants of the subdivision declaration rather than on the application of any Mentor zoning ordinance. Thus, the court of appeals entered summary judgment in favor of the city.

The Supreme Court of Ohio reversed. The argument that the subdivision declaration constituted a purely private matter was erroneous. The Mentor Code of Ordinances requires a subdivider to submit plats for approval by the city. Since some municipal approval of the subdivision is contemplated, restrictive covenants contained in the subdivision declaration are not completely private. Thus, insofar as Mentor approved the creation of the subdivision and applied covenants in the subdivision declaration to deny Duncan's application to build a single-family residence, a compensable taking might have occurred. Since genuine issues of material fact remain, the judgment of the court of appeals was reversed and remanded for further proceeding

A concurrence emphasized that no determination had been made as to whether a regulatory taking had occurred.

Comment 1: A concurrence emphasized that the court was not deciding that the claimant had indeed established that a regulatory taking had occurred. The claimant had bought the property apparently at a tax foreclosure sale for $1000, and claimed that he had no notice of any ownership claims of a homes association. The court noted that the recorded declarations likely provided such notice. The question remains how the property wound up in Duncan's hands. Perhaps there was a failure on the part of the association to pay the taxes or perhaps there was the plain ole' tax commissioner's error.

Comment 2: What the editor finds of interest here is the actual fact of a planning agency relying upon private land use restrictions in making its decision. Some time ago, the editor opined that agencies commonly look to private restrictions in making decisions on items like variances, and he was excoriated by a number of members of the DIRT list for his naivete. (Not the first time.) Many DIRTers stated that in their experience land use agencies totally ignored the any private restrictions.

Comment 3: What was really going on the case, the court suggests very obliquely was that the claimant was playing dog in the manger to get the city to buy his property. The property was adjacent to a stream that provided flood control, and the city apparently was interested in purchasing it. The court noted that the owner had refused an offer to acquire the property equal to the $1000 the claimant paid for the property. It doesn't look much like the claimant is going anywhere with this case, despite his victory here.

ZONING AND LAND USE; VARIANCES; STANDARD: Zoning boards have broad discretion in considering applications for variances, and judicial review is limited to determining whether the board action was illegal, arbitrary or an abuse of discretion. ***Plotnick v. Wok's Kitchen Inc., 800 N.Y.S.2d 37 (A.D. 2 Dept. 2005).*** The petitioner in this Article 78 proceeding appealed the zoning board's denial of its application for a variance to permit the development of single-family residences in a district that requires each lot to be at least 18,000 square feet. The board determined that the variance would undesirably alter the neighborhood character, would adversely impact the conditions of the neighborhood and that feasible alternatives had not been pursued. In recognizing the board's wide discretion, the court held that this was a rational basis for the board's determination and that the ruling should not be disturbed.

Comment: The first two bases for the decision here are so general that they seems impossible to review, and other courts have so found. But the third test, whether there are feasible alternatives that would not require a variance, does seem an acceptable, if uncomfortable, basis for decision.