Quarterly Report on Current Developments in Real Estate Law

October 1, 2006 through December 31, 2006

Sponsor:

ABA Section on Real Property
Probate & Trust Law
American Bar Association

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Statement of Editorial Policy:

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.

The editors hope to provide a comprehensive review of significant new developments, but obviously they cannot warrant that every new case is reported. Further, readers should be aware that the editors specifically eliminate from coverage cases that are of interest primarily to lawyers within a given state. Thus, significant interpretations of state statutes or constitutions, even if of critical importance to local practitioners, may not appear in the Report. Readers should rely upon update services provided by state or local sources to stay current on such developments.

The editor of the Report alone controls the content of the case reports section of the Report and, for the most part, prepares the comments and criticisms added to the case summaries. The views expressed in the Report have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, accordingly, should not be construed as representing the policy of the American Bar Association. Similarly, they are not the view of the Section of Real Property, Probate & Trust Law.

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*The editor frequently revises reports and occasionally adds comments not submitted by a contributor. Time constraints do not permit contributors to review and ratify such changes. Therefore, inaccuracies in the reports and the content of many comments are the responsibility of the editor, and not necessarily of the identified contributor.

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ADVERSE POSSESSION; REQUIREMENT OF CONTINUOUS POSSESSION: The use of a property on a seasonal basis to operate a canoe rental and camping business is sufficient to constitute notice in establishing an adverse possession claim. ***Robinson v. Robinson, 825 N.Y.S.2d 277 (A.D. 3 Dept. 2007)***. Owners of a canoe rental and camping business ("Business Owners") conducted operations for a five-month period each year. During this time, they erected signs, cut the grass, transported canoes, blocked trespassers, constructed roads and used and maintained campsites. From time to time, family members and neighbors would use the property recreationally. Business Owners brought an action against the record owner ("Record Owner") to assert title to the riverfront property by deed and adverse possession. They sought to enjoin the Record Owner permanently from interfering with the property. The court held that use of the property by the Business Owners was open, hostile and notorious and therefore sufficient to convey notice of adverse possession claim to the Record Owner.

Furthermore, despite the seasonal nature of the business, the use was continuous and uninterrupted in nature and thus did not defeat the adverse possession claim, nor did the fact that neighbors and family members occasionally used the property recreationally. Finally, neither the fact that Business Owners failed to pay real estate taxes during the adverse possession period nor their subjective belief that Record Owner was the rightful owner defeat the adverse possession claim.

ALTERNATIVE DISPUTE RESOLUTION; ARBITRATION; CONTRACTS: If written notice of an arbitration hearing does not describe the nature of controversy and the remedy sought, the arbitrator lacks the authority to address and impose any extraordinary remedy not described in the arbitration notice. ***Block v. Plosia, 390 N.J. Super. 543, 916 A.2d 475 (App. Div. 2007)***

Homeowners hired a contractor to complete an addition to their residence pursuant to an architect's blueprints and specifications. The contractor did not complete the work consistent with the architect's plans, and the work remained incomplete past the promised completion date. The homeowners had to retain the same architect to prepare "as built" plans to satisfy the municipal inspector, and to get another contractor to complete the work, causing them to expend substantial funds. The homeowners made the contractor aware of their consequential costs, which were disputed by the contractor.

The homeowners and the original contractor eventually agreed to submit their dispute to binding arbitration, and signed an arbitration agreement. The agreement called for the advance submission of a limited statement of issues. The homeowners claimed $40,227.90, which included costs to remedy the non-compliant work and complete the construction project to a compromised but usable condition, and attorney fees during the course of their dispute with the contractor. The arbitrator found that the contractor breached its contractual obligations through its untimely, incomplete, and unworkmanlike performance of the construction, and calculated homeowner damages in the amount of $31,457.91 for past incurred costs and estimated future expenses. He also concluded that the contractor violated the New Jersey Consumer Fraud Act, and awarded treble damages, thereby calculating a total award of $94,373.73. The homeowners filed suit to confirm this award which was affirmed by the lower court, except that the attorney fee component of the total award was not trebled. The contractor appealed.

The Appellate Division concluded that the consumer fraud issues implicated by the contractor's construction work were not properly submitted to the arbitrator such as to afford fair notice to the contractor before the arbitration took place. Such notice was found vital as a matter of fundamental fairness. The Court observed that the homeowners never filed a court pleading or arbitration statement notifying the contractor that it was invoking the Consumer Fraud Act and the Act's remedies of treble damages and fee shifting. The Court stated that the first time the contractor learned of his exposure in that regard was through the arbitrator's written decision. It held that written notice of an arbitration hearing must describe the nature of the controversy and the remedy sought. Therefore, in this matter, the Court concluded that the arbitrator lacked the authority to address and impose an extraordinary remedy such as treble damages, without definition by the parties in their description of the issues involved. Accordingly, the Court modified the award to reflect the traditional compensatory damages for the breach of contract. The Court also upheld the attorney fee component of the total compensatory damage figure.

ALTERNATIVE DISPUTE RESOLUTION; ARBITRATION; TITLE INSURANCE: Title insurance policy's arbitration clause was not enforceable against insured because it was not included or referenced in preliminary title report. ***Kleveland v Chicago Title Ins. Co., 141 CA4th 761, 46 CR3d 314 (2006***)

Kleveland and AOK Land Company (collectively, Kleveland) purchased a title insurance policy from Chicago Title on the basis of a preliminary title report that described the property to be insured, the coverage to be afforded, and exceptions and exclusions. The preliminary title report did not indicate the policy would include an arbitration clause. The cover sheet of the preliminary report identified the form of title insurance as an American Land Title Association (ATLA) policy. The ATLA policy had an arbitration clause.

Chicago Title issued a California Land Title Association Standard Coverage Policy (CLTA) instead of the policy specified in the preliminary report. The CLTA policy contained an arbitration clause.

Kleveland sued Chicago Title after discovering an easement on the property not mentioned in the preliminary title report. Chicago Title moved to compel arbitration based on the clause in the CLTA policy. The trial court denied the motion.

The court of appeal affirmed. Chicago Title argued that Kleveland was bound by the arbitration clause in the CLTA policy because Kleveland received a copy of that policy and did not object.

Chicago Title relied on the rule that an insured has a duty to read the policy and cannot thereafter complain that the terms were unknown. The court noted, however, that that rule does not apply to title insurance. Title insurance has a one time premium and remains in effect as long as the insured owns the property; the insured may not cancel the policy and switch to another carrier without forfeiting the premium. Accordingly, the process of obtaining title insurance contemplates the receipt, before close of escrow, of a title report that sets forth the conditions on which the issuer is willing to issue its title policy. The insured's approval and acceptance of the conditions set forth in the preliminary report creates a binding contract based on the terms set forth in the report and any materials that are incorporated by reference. Therefore, whether the insured is bound by an arbitration clause depends on whether that term was set forth in the preliminary report or incorporated therein by reference.

The preliminary title report did not contain an arbitration clause or explicitly state that such a clause would be contained within the policy to be issued. It did refer to the type of policy to be issued, and the insurer argued that such reference was sufficient to establish the clause. The court noted that incorporation by reference requires that:

> "The reference to another document is clear and unequivocal; . . . [the reference is called to the attention of the other party and the other party consents to that term; and] . . . the terms of the incorporated documents are known or easily available to the contracting parties."

Chicago Title argued that the preliminary report incorporated the ALTA policy and its arbitration clause by reference because it mentioned that policy by name. However, the ALTA policy never went into effect. The only arbitration clause that could conceivably be enforced was the one in the CLTA policy that was actually issued, but that policy was not clearly and unequivocally referred to in the contract.

Although Chicago Title contended it was unfair to deny arbitration when the clause in the CLTA policy was virtually identical to the arbitration clause in the ALTA policy, it was unreasonable to rely on an arbitration clause in a nonexistent policy to deny Kleveland the right to a jury trial. Chicago Title, the drafter of the preliminary report, was in the best position to avoid this problem by including the arbitration clause in the report itself.

Reporters Comment: Is a party bound to arbitrate when the preliminary title report does not itself contain an arbitration clause, but says that an ALTA title policy will be issued which policy does contain an arbitration clause and then issues a CLTA policy instead, which also contains an arbitration clause, although one differently worded from the ALTA clause?

The clause in the originally promised ALTA policy would have said:

> "11. ARBITRATION:
>
> a. If permitted in the state where the Land is located, You or We may demand arbitration.
> b. The arbitration shall be binding on both You and Us. The arbitration shall decide any matter in dispute between You and Us.
> c. The arbitration award may be entered as a judgment in the proper court.
> d. The arbitration shall be under the Title Insurance Arbitration Rules of the American Arbitration Association. You may choose current Rules or Rules in existence on Policy Date.
> e. The law used in the arbitration is the law of the place where the Land is located.
> f. You can get a copy of the Rules from Us."

The clause in the CLTA policy actually issued instead said:

> "13. ARBITRATION. Unless prohibited by applicable law, either the Company or the Insured may demand arbitration pursuant to the Title Insurance Arbitration Rules of the American Arbitration Association. Arbitrable matters may include, but are not limited to, any controversy or claim between the Company and the insured arising out of or relating to this policy, any service of the Company in connection with its issuance or the breach of a policy provision or other obligation. All arbitrable matters when the Amount of Insurance is $1 million or less shall be arbitrated at the option of either the Company or the insured. All arbitrable matters when the Amount of Insurance is in excess of $1 million shall be arbitrated only when agreed to by both the Company and the insured. Arbitration pursuant to this policy and under the Rules in effect on the date the demand for arbitration is made or, at the option of the insured, the Rules in effect at Date of Policy shall be binding upon the parties. The award may include attorneys' fees only if the laws of the state in which the land is located permit a court to award attorneys' fees to a prevailing party. Judgment upon the award rendered by the Arbitrator(s) may be entered in any court having jurisdiction thereof. The law of the situs of the land shall apply to an arbitration under the Title Insurance Arbitration Rules. A copy of the Rules may be obtained from the Company upon request."

Notwithstanding linguistic and stylistic differences, both versions provided that:

Either party could demand arbitration; that such arbitration would be conducted under the insured's choice of current or earlier AAA rules, obtainable from the company; that the law of the land (situs) would apply; and that the award would be binding and could be entered as a judgment in court.

As to differences: The ALTA clause said arbitration could cover "any matter in dispute", while CLTA would cover "any controversy or claim arising out of or relating to the policy"; the difference is hard for me to discern. CLTA added that attorney fees would be awarded only if state law so provides, whereas ALTA was silent (and I know of no California law awarding fees). Finally, CLTA included a requirement that both parties agree to arbitrate disputes of over $1 million, which ALTA did not. (The briefs do not show the size of the claim, but the preliminary title report shows annual property taxes of under $600, which leads me to surmise that the claim did not fall into the over $1 million category.) Given the policies" similarities, I would say that the requirement that reference to another document be "clear and unequivocal" understates the real standard. These clauses were "virtually identical" in substance, yet incorporation was denied. Literal, not virtual, identity is the measure.

The opinion suggests that Chicago Title "could have simply included an arbitration clause in the report itself" (141 CA4th at 765), but I wonder: How effective would it have been if the clause in the preliminary report had differed from the clause in the policy? It would probably be safer for both clauses in a two document transaction such as this to include savings provisos to the effect that if there is any discrepancy between their words, the insured has the option of selecting the version he or she likes best.

Editor's Comment: To the editor, an agreement to arbitrate "any matter in dispute between the parties" is potentially much broader than an agreement to arbitrate only policy matters. Further, if the "any matters" arbitration agreement were to be given the broad reading that it suggests, the $1 million limit might become relevant as well.

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

ALTERNATIVE DISPUTE RESOLUTION; ARBITRATION; UNCONSCIONABILITY: Developer's preprinted real estate contract was not a contract of adhesion, but provisions of the arbitration clause requiring one party to pay all costs of arbitration and contained in the contract were substantively unconscionable and, therefore, unenforceable. ***State ex rel. Vincent v. Schneider, 194 S.W.3d 853 (Mo. 2006)***.

The plaintiffs were purchasers of single family homes from McBride & Son Homes, Inc. Each plaintiff executed a preprinted written contract which contained a provision that gave McBride the unilateral right to require the plaintiffs to submit any claim arising out of the contract or the home to binding arbitration. The arbitration provision also provided that the "arbitrator shall be selected by the President of the Homebuilders Association of Greater St. Louis" and "Purchaser shall be liable to Seller for all court, arbitration and attorney's fees and costs incurred by Seller in enforcing this provision."

Each plaintiff initialed the arbitration provisions in their respective contracts to indicate that they had read, understood and agreed to the terms. The plaintiffs later discovered problems with their newly-purchased homes and filed a lawsuit against McBride. McBride sent a letter to plaintiffs stating that (i) McBride was requiring resolution of the claims by binding arbitration, (ii) plaintiffs were required to pay McBride's costs of enforcing the arbitration provision, and (iii) the president of the Homebuilders Association was also the president of McBride and was no longer willing to appoint an arbitrator.

McBride then filed a motion to compel arbitration, which was granted by the trial court. The plaintiffs sought a writ of mandamus from the Supreme Court to compel the trial court to deny McBride's motion to compel. Plaintiffs argued that the real estate contracts they signed were contracts of adhesion and, therefore, unenforceable pursuant to Mo. Rev. Stat. 435.350. Plaintiffs, however, failed to offer any proof that the contracts they signed were contracts of adhesion, and the Court noted that plaintiffs could not rely solely on the fact that the contracts in this case were pre-printed to prove they were contracts of adhesion.

Plaintiffs also argued that the arbitration clause in the contract was unconscionable for three specific reasons: 1) it gave only McBride the right to select arbitration; 2) it

gave the president of the Homebuilders Association the sole discretion to choose the arbitrator; and 3) it placed all costs of the arbitration on plaintiffs. The Court rejected plaintiffs' first argument, holding, as a matter of first impression, that since there was consideration as to the whole agreement, the lack of mutuality of obligation of the arbitration clause does not make it invalid.

The Court did, however, agree with plaintiffs' second and third arguments. It determined that the arbitration clause was unconscionable because (i) the individual with sole discretion to select an arbitrator was in a position of bias and (ii) the cost-shifting provision of the clause essentially granted one party to the contract immunity from legitimate claims arising under the contract. Thus, these two provisions of the arbitration clause were unenforceable. The Court held that the rest of the arbitration provision is enforceable as long as the arbitrator is selected by the trial court and the costs of arbitration are allocated as provided in the arbitrator's award.

ATTORNEYS' FEES; BANKRUPTCY: U.S. Supreme Court rules that Bankruptcy Code does not disallow contract based claims for attorneys' fees based solely on fact that fees at issue were incurred litigating issues of bankruptcy law. ***Travelers Casualty & Surety Co. of America v. Pacific Gas & Electric Co., 127 S.Ct. 1199 (2007).***

An issue that has been litigated (with conflicting results) is whether the Bankruptcy Code disallows a lender's contract based claims for attorneys' fees based solely on the fact that the fees at issue were incurred litigating issues of bankruptcy law. On March 20, the U.S. Supreme Court, in *Travelers Casualty & Surety Co. of America v. Pacific Gas & Electric Co.,* 127 S.Ct. 1199 (2007), settled this issue by concluding that it does not. Prior to the bankruptcy proceedings in this case, Travelers Casualty & Surety Co. of America ("Travelers"), a creditor of the debtor, had issued a surety bond on the debtor's behalf guaranteeing the debtor's payment of state worker's compensation benefits. Travelers filed a claim in the debtor's subsequent bankruptcy proceeding to protect itself in the event of the debtor's future default of payment of the workers' compensation benefits. The bankruptcy court, the U.S. District Court, and the Ninth Circuit Court of Appeals all denied Travelers' application for work done negotiating the language in the debtor's post petition reorganization plan and disclosure statement that provided for Travelers' right of indemnification and indemnity in the event of default. But the U.S. Supreme Court held that Travelers was not precluded from filing an unsecured claim for its contractual attorneys' fees, merely by virtue of the fact that the fees sought had been incurred in litigating issues of federal bankruptcy law.

This decision by the Supreme Court abrogated a prior holding by the Ninth Circuit, *In re Fobian*, 951 F.2d 1149, which had held that where the ability to recover attorneys' fees was basically one interpreting federal bankruptcy law, attorneys' fees could not be recovered even though the dispute arose out of a contract containing a provision for the recovery of such fees. This rule (called the "*Fobian* rule") was contrary to the rule applied by the Fourth Circuit Court of Appeals in *In re ShangriLa, Inc.*, 167 F.3d 843, 84849 (C.A.4 1999), and the SuprmeCourt therefore granted certiorari in the Travelers Casualty & Surety Co. case to resolve the conflict.

The Supreme Court acknowledged that generally the "American Rule" does not award attorneys' fees to the winner of litigation, but held that the rule does not apply when where the parties have entered into an enforceable contract allocating attorneys' fees. The Supreme Court stated that the ability to recover attorneys' fees was basically one of state law and that "unless some federal interest requires a different result, there is no reason why such interests should be analyzed any differently simply because an interested party is involved in a bankruptcy proceeding." *Id.* at 1205 (quoting *Butner v. United States,* 440 U.S. 48, 57 (1999)). The court also found that there was nothing in the Bankruptcy Code that supported the Fobian rule and that the Bankruptcy Code simply directs bankruptcy courts to determine whether applicable state law would permit the recovery of attorneys' fees and to apply that same result to disputes in bankruptcy proceedings. As a result of the Supreme Court's ruling, a creditor having a legitimate claim can now safely include attorneys' fees (assuming the contract between the parties allows such fees) as part of its bankruptcy claim whether or not the fees arise out of litigation involving issues of federal bankruptcy law (but the resultant increase in the amount of the claim will not alter the relative priority or ultimate collectability of the claim).

Reporter's Comment 1: Interestingly, the Supreme Court refused to consider the debtor's argument that § 506(b) of the Bankruptcy Code disallows unsecured claims for contractual attorneys' fees where – as in this case – the creditor's entire claim was unsecured. (Section 506(b)

authorizes claims for contractual attorneys' fees to the extent the creditor is oversecured, but disallows such claims to the extent the creditor is either not oversecured or completely unsecured.) The court stated that the debtor had not raised or addressed this argument in the courts below and that the debtor "has failed to identify any circumstances that would warrant an exception to that rule in this case." Id. at 1207. The court further stated that in this particular case "[w]e granted certiorari to resolve a conflict among the lower courts regarding the *Fobian* rule, which is analytically distinct from, and fundamentally at odds with, [the debtor's] reading of § 506." Id. The court reasoned that such a reading of § 506 "would prohibit all unsecured creditors from recovering contractual postpetition attorneys' fees in bankruptcy proceedings – even if those fees were incurred while litigating issues of state law." *Id.* at n.4. The court was careful, however, to state that "[w]e conclude only that the Court of Appeals erred in disallowing that claim based on the fact that the fees at issue were incurred litigating issues of bankruptcy law." *Id.* at 1208.

Reporter's Comment 2: Section 506(b) of the Bankruptcy Code permits a secured creditor, to the extent that its claim is oversecured, to collect interest on such claim and any reasonable fees (including attorneys' fees, costs, and charges) that are provided for in the loan documents. *See, e.g., In re Foertsch,* 167 B.R. 555, 562 (Bankr. D.N.D. 1994) (holding, in context of request for recovery of attorneys' fees, that in order to recover "fees, costs and charges" under § 506(b), creditor must establish: (1) that it is oversecured in excess of the amount requested; (2) that the amount requested is reasonable; and (3) that the agreement giving rise to the claim provides for recovery of the fee, cost or charge requested); *In re Udhus,* 218 B.R. 513, 517 (9th Cir. B.A.P. 1998) (same, with respect to claim by creditor for "administrative costs"); *In re Direct Transit, Inc.,* 226 B.R. 198, 201, 203 (8th Cir. B.A.P. 1998) (ruling that § 506(b) permits a claim for additional charges if the claim is oversecured, the charge is provided for in the agreement, and it is reasonable); *In re Hyer,* 171 B.R. 67, 70 (Bankr. W.D. Mo. 2004) (holding that oversecured creditor is entitled to enforce valid contractual obligation for payment of attorneys' fees where an attorneys' fee provision is included in the debt instrument, as long as the fees requested are reasonable.)

Reporter's Comment 3: The oversecured creditor generally can collect attorneys' fees even if applicable state law prohibits the collection of such fees by the creditor. *See, e.g., In re Hyer, supra,* 171 B.R. 69 (stating that "506(b) allows an oversecured creditor to recover attorneys' fees if they are provided in the security agreement, notwithstanding Kansas law." [Note: The Kansas Legislature amended Kan. Stat. Ann. § 582312 in 1994, to allow the inclusion of attorneys' fee provisions in notes, mortgages or other credit agreements. 1994 Kan. Sess. Laws Ch. 276, § 3]); *In re American Metals Corp.*, 31 B.R. 229, 234 (Bankr. D. Kansas 1983) (same); *In re Schriock Const., Inc.,* 104 F.3d 200, 203 (8th Cir. 1997) (holding that attorneys' fees provisions in loan documents are enforceable in bankruptcy even though state law prohibits them).

Reporter's Comment 4: Another issue that bankruptcy courts have wrestled with is whether the "reasonableness" of the charges under § 506(b) is determined by state or federal law – or both. *See, e.g., In re Dixon, 228* B.R. 166, 177 (Bankr. W.D. Va. 1998) ("[t]he reasonableness of charges under § 506(b) is determined by reference to the relevant state contract law"). *But see In re 268 Ltd.*, 789 F.2d 674, 67677 (9th Cir. 1986) (applying single federal standard of "reasonableness" with respect to issue of whether an attorneys' fees provision is allowable under § 506(b)); *cf. In re Hudson Shipbuilders, 794* F.2d 1051, 1058 (5th Cir. 1986) (holding that fees otherwise enforceable under state law were still subject to § 506(b)'s requirement that fees be "reasonable"); *In re Hyer, supra,* 171 B.R. at 71 ("11 U.S.C. § 506(b) is not dependent upon state law. 11 U.S.C. § 506(b) allows the recovery of reasonable attorneys' fees to an oversecured creditor if they are provided for in the underlying agreement, which is the case herein").

Reporter's Comment 5: Bankruptcy courts also have reached conflicting results with respect to the issue of whether § 506(b) applies only to postpetition(as opposed to prepetition and postpetition) fees and charges. *See, e.g., In re Nunez,* 317 B.R. 666, 670 (Bankr. D. Pa. 2004) ("We hold that section 506(b) applies only to post petition interest, fees and costs sought as part of a secured claim. Quite simply, interest, fees and costs arising prepetition are already a part of a secured creditor's proof of claim in the first instance, rendering section 506(b) inapplicable"). *But see In re Hyer, supra,* 171 B.R. 70 ("When an oversecured creditor is entitled to enforce a valid contractual obligation for the payment of attorneys' fees, 11 U.S.C. § 506(b) applies whether the attorneys' fees were incurred before or after the filing of the

bankruptcy petition."). *Cf. Laxa v. United States (In re Laxa),* 312 B.R. 394, 398 (D. Ariz. 2003) ("While post petition charges, including penalties, may be included in a secured claim only as authorized by section 506(b), pre petition charges, including penalties, are properly included as part of the secured claim" (citations omitted)). See also *In re Leatherland Corp.*, 302 B.R. 250, 25657 (Bankr. D. Ohio 2003) ("Even though they all assert they are interpreting the plain meaning of the statute . . . courts have arrived at differing conclusions as to whether § 506(b) applies to prepetition as well as to postpetition fees, costs and charges") (citations omitted).

Reporter's Comment 6: It is incomprehensible that the debtor's attorneys did not argue, at any stage during the proceedings in the lower courts, the applicability and relevance of § 506(b) of the Bankruptcy Code in this particular matter. The debtor was therefore barred from raising this important issue before the Supreme Court, even though Travelers' entire claim was unsecured. The Supreme Court seems to have vacillated on how it would have ruled if this issue had been properly raised, and was careful to clearly limit its holding to overturning the *Fobian* rule.

Reporter's Comment 7: Lenders should be careful to request specifically, in state foreclosure proceedings, that attorneys' fees and other charges and fees (such as a prepayment premium) provided for in the note and/or mortgage be specifically included in the foreclosure judgment so that the state court will allow such fees and charges and bankruptcy courts will permit collection of such fees and charges if a bankruptcy proceeding is subsequently filed by or against the mortgagor. *See, e.g., In re McClung* (Bankr. D.Kan., Dec. 11, 2003), ("If [the lender] wished to assert its right, under the note and mortgage that were the subject of the suit, to a prepayment penalty, it was required to raise the issue in the foreclosure proceeding it commenced in state court, or be forever barred").

The reporter for this item was Jack Murray of the First American Title Insurance Company in Chicago.

ATTORNEY'S FEES; "PARALLEL RIGHTS" STATUTE: Although a guaranty agreement permitting the guaranteed party to recover attorney's fees is void *ab initio* and can provide no contractual basis for recovery of fees for the guaranteed party, the guarantor nevertheless can recover attorney's fees under the Utah "parallel rights" statute, which permits both parties to recover fees where they have contracted for only one party to recover such fees. ***Bilanzich v. Lonetti 2007 WL 817495 (Utah 2007)***

This case has some interesting facts and a somewhat unsettling result, depend upon how far the lower court takes the Supreme Court's mandate on fees.

A corporation borrowed about $1.8 million from Lonetti. When it failed to pay, negotiations ensued during which an agreement was reached that the note would be recast to include accrued interest and other debts, for a total amount of about $2.2 million, and additional financing would be obtained to permit the corporation to continue to operate and repay the debt. Bilanzich agreed that, in exchange for an interest in the newly financed corporation, he would guarantee the debt. He executed a guarantee and deposited it into escrow pursuant to a contract that stated "[i]f financing is not obtained, the closing will not occur, all items in escrow will be returned to the party depositing them, and Lonetti will foreclose and realize on security."

The financing was never obtained, and all apparently it was clear that the guarantee agreement should have been returned to Bilanzich, but instead it was delivered to Lonetti, (mistake number one) who later assigned it, along with the note and mortgage, to a controlled corporation. There is no indication in the case that the corporation truly intended to sue on the guarantee. On the other hand, it doesn't appear that Lonetti was all that quick in returning the wrongfully delivered guarantee to Bilanzich either. Certainly there is a tale here, but it remains untold in the court's opinion.

Bilanzich brought a lawsuit against the borrower corporation and Lonetti. The lawsuit sought rescission of the guarantee and also included a claim of unjust enrichment against Lonetti and its corporation. The corporation responded (foolishly, from what we know based on the case report) with a suit on the guarantee. Mistake number two.

Bilanzich sought and obtained partial summary judgment in his favor on the rescission claim, and the parties settled the balance of the lawsuit with Bilanzich dismissing his claims and the Lonetti's and their corporation agreeing not to appeal the summary judgment. The settlement agreement apparently did not include a clear settlement

of attorney's fee claims. Mistake number three. Whether some language in the agreement did indeed preclude a fee claim is a mistake that this decision specifically reserved for later adjudication.

The trial court found that the fact that the guarantee was void rendered any claim for attorney's fees also void. The appeals court agreed, but the Utah Supreme Court, with two dissenters, overturned these rulings and remanded with instructions that attorney's fees could be awarded under Utah's "parallel rights" attorney's fee statute: "[a] court may award costs and attorney's fees to either party that prevails in a civil action based upon any promissory note, written contract, or other writing . . . when the provisions of the promissory note, written contract, or other writing allow at least one party to recover attorney's fees.

The Supreme Court stated that Bilanzich expended attorney's fees in response to the Lonetti's assertion that the guarantee provided them a legal right to recovery. This suggests that the subtext of this dispute was that Bilanzich felt compelled to seek rescission because Lonetti and the corporation were indeed taking the position that he was bound by the guarantee.

The court noted that the fee statute did not compel the awarding of attorney's fees, and that the court should take into account its purpose to create a "level playing field" for parties disputing about the debt instruments and guarantees.

Comment 1: The editor likes these statutes. A one-sided fee agreement provides a powerful club permitting one side to a dispute to push around the other side. The editor is fine with bargaining imbalance resulting in a contract favoring one side, but the stronger side shouldn't also get the benefit of being able to discourage the other side from litigating when ambiguities or disagreements later arise.

Comment 2: Here, however, we have the somewhat bizarre outcome of an agreement being found void, and therefore providing no basis for the beneficiary of the guarantee obtaining attorney's fees, but nevertheless the court views the other party – the guarantor – as eligible to get fees simply because the void contract provided for them. The editor disagrees. There was no agreement, so the statute can't be invoked. It is true that Bilanzich executed a guarantee, and it was delivered, but the circumstances of delivery rendered the guaranty totally void. It was the equivalent of a forged document. When the editor sees nondelivery cases involving deeds, he often asks himself the question: "What would have been the outcome if the document was forged?" The court should have asked itself the same question here. The dissent got it right.

As indicated above, however, the editor isn't that sympathetic to the Lonetti side here. Although, as indicated, there may be facts of which we are unaware. But the court says that Lonetti's side knew that the guarantee had been delivered out of escrow in error. It knew that the contract provided that the guarantee kicked in only if financing had been obtained, and that the financing had not been obtained.

BANKRUPTCY; ATTORNEYS' FEES: U.S. Supreme Court rules that Bankruptcy Code does not disallow contract based claims for attorneys' fees based solely on fact that fees at issue were incurred litigating issues of bankruptcy law. ***Travelers Casualty & Surety Co. of America v. Pacific Gas & Electric Co., 127 S.Ct. 1199 (2007),*** discussed under the heading: "Attorney's Fees; Bankruptcy".

BANKRUPTCY; ATTORNEY'S FEES; FORECLOSURE: In a bankruptcy case, a mortgagee's claim for the trustee's fees and other expenses is not necessarily limited to the amounts embodied in the judgment of foreclosure prior to the bankruptcy case, especially where the bankruptcy trustee has acted in such a way so as to cause the mortgagee to incur additional fees and costs. ***In Re Price, 2007 WL 430765 (U.S. Bkrtcy. D. N.J. 2007).***

Homeowners fell behind in their mortgage payments and the mortgagee filed a foreclosure action. A judgment of foreclosure was entered, but before the sheriff's sale was commenced, the homeowners filed for bankruptcy under Chapter 11. At the outset of the case, the homeowners, now bankruptcy debtors-in-possession, agreed to make regular monthly payments to the mortgagee as adequate protection payments. Then the mortgagee submitted a claim in the bankruptcy case.

For several months, the debtors paid the mortgagee according to the agreed terms. Thereafter, the debtors submitted a check that was twice returned for insufficient funds. In response to the default, the mortgagee filed a motion for relief from the automatic stay. The motion was denied and the mortgagee was ordered to accept

subsequent payments. Over the course of the following three years, the debtors continued to submit payments to the mortgagee, many of which were returned due to insufficient funds. On eight separate occasions the mortgagee sought relief from the stay to proceed with the foreclosure action. Each time, the debtors, or the trustee subsequently appointed to represent the debtor's bankruptcy estate, succeeded in convincing the Court to deny the mortgagee's motion. In support of its opposition to the later motions, the trustee argued that the property at issue would provide a significant recovery for the bankruptcy estate once the trustee was able to gain approval of specified subdivisions from the planning board.

Eventually, the trustee was able to negotiate a sale price for the property in significant excess of the mortgagee's allowed secured claim. The Court approved the sale and ordered the mortgagee to submit a statement detailing the amounts it was owed. In compliance with the Court's order, the mortgagee submitted a statement which included attorney's fees and costs incurred during the pre-bankruptcy foreclosure action. The trustee paid the amounts delineated in the mortgagee's statement, but with a "reservation" of claims and rights in connection with some of the fees and costs. Essentially, the trustee disputed whether the mortgagee was entitled to recover fees and costs provided for in the initial note and mortgage, but not reflected in the judgment of foreclosure.

Then, the trustee commenced an adversary proceeding within the bankruptcy case seeking recovery of the attorney's fees, interest, late fees, sheriff's fees, and real estate taxes. In support of its claims for recovery, the trustee asserted causes of action for accounting and turnover, legal fraud, equitable fraud, and conversion. The mortgagee filed a motion for summary judgment and the Court granted the motion in its favor.

Before addressing the merits of the summary judgment motion, however, the Court addressed the trustee's contention that the mortgagee's claim was limited to that embodied in the judgment of foreclosure prior to the bankruptcy case. The trustee's relied on a Court of Appeals case in which a mortgagee was precluded from asserting claims based on the terms of the mortgage agreement because the lending agreements had "merged" into the final judgment of foreclosure. Hence the trustee argued that the fees and costs at issue arose pursuant to the mortgage agreement and had not been adjudicated within the judgment of foreclosure on the mortgage; therefore, the mortgagee should be precluded from adding the fees to its allowed secured claim during the bankruptcy case. The Court rejected this argument because at the time the homeowners filed for bankruptcy, the mortgagee's claim had not been satisfied – the sheriff's sale was thwarted by the automatic stay triggered by the bankruptcy filing. In theory, the mortgagee could have petitioned the lower court conducting the foreclosure for satisfaction of the fees and costs in question, but any such petition was barred by the automatic stay. The mortgagee was not negligent, it was simply saddled with the lower court's many rejections of its motions for relief from the stay.

Moreover, the Court held, the trustee should not be permitted to claim that the mortgagee was not entitled to additional fees and costs in connection with the foreclosure after the property was sold when, prior to the sale, the trustee took no such position. The equitable principle of "quasi-estoppel" barred the trustee from prevailing on this inconsistency. "Quasi-estoppel," the Court explained, precludes a party from asserting a position contrary to a prior position, pursuant to which he accepted a benefit that resulted in prejudice to another party, when the circumstances are such that it would be unconscionable for the inconsistency to stand. Here, the trustee's position prior to the sale was that it needed more time to negotiate the best sale price which, in turn, would serve to benefit all creditors – the mortgagee included. By asserting this position, the trustee was afforded the benefit of time and of staving off the mortgagee's efforts to pursue its foreclosure remedies. The trustee's change in position, opposing the mortgagee's efforts to pursue its remedies, prejudiced the mortgagee to an extent that the unfairness was obvious and warranted an equitable remedy. Thus, the mortgagee was not precluded from asserting its claims for fees and costs. Since the mortgagee held an allowed secured claim in the bankruptcy proceeding and it was over-secured by the property at issue, the bankruptcy court agreed to retain jurisdiction to hear arguments on the merits.

Turning then to the mortgagee's motions, the Court granted summary judgment in the mortgagee's favor. It dismissed the trustee's claims of legal fraud, equitable fraud, and conversion. The trustee could not meet its burden on legal fraud because it could not prove that the trustee relied on the mortgagee's representations, and it

could not prove equitable fraud because the trustee did not reasonably rely on a material misrepresentation of fact. Rather, as the undisputed facts revealed, the bank's payoff statement was based on particularized business records which had provided to the trustee for review. Further, the trustee could not prove conversion because the bank lawfully came into possession of the money paid to it by the trustee. Regarding the trustee's "accounting and turnover" claim, the Court held that a trial would be necessary as to the reasonableness of the attorney's fees, the appropriate rate of interest and accrual, as well as the appropriate principal balance for such calculations in light of the bank's misapplication of the adequate protection payments to attorney's fees.

BANKRUPTCY; REDEVELOPMENT AGREEMENTS: A property owner cannot reject a redevelopment settlement agreement by filing a bankruptcy petition where the municipality has already substantially performed all of its obligations under the agreement, because such an agreement is not executory and therefore not subject to rejection. ***In Re S.A. Holding Co., LLC, 2006 WL 3804558 (U.S. Bkrtcy. D. N.J. December 22, 2006)***

A dispute between an adult nightclub and a municipality was settled when it was agreed that the nightclub would continue to operate as a "go-go club" for two years in exchange for then allowing the municipality "to designate the property for redevelopment and establish[ment] [of] a redevelopment plan." This agreement was memorialized in a settlement agreement accepted by a court. The agreement was modified two years later. Three years after that, the municipality adopted the redevelopment plan by enactment of an ordinance. The club did not oppose the municipality's action. Then, the municipality returned to a New Jersey court to enforce the settlement agreement. "Specifically, the [municipality] sought to close the business as was agreed and for payment of its counsel fees and costs. The [club] for the first time sought to challenge the redevelopment plan." A judgment was entered in favor of the municipality. It "directed the business to close immediately." The matter dragged on until the day before an evidentiary hearing was to take place, the club filed a bankruptcy petition for relief under Chapter 11 of the Bankruptcy Code. This automatically stayed the state court action. In its bankruptcy proceeding, the club sought to reject the settlement agreement as an executory contract. "The Bankruptcy Code does not define the term 'executory contract,' nor does [section 365(a)] indicate the phrase's intended scope. ... The legislative history of [section 365] indicates that '[t]hough there is no precise definition of what contracts are executory, it generally includes contracts on which performance remains due to some extent on both sides'." Here, the Court noted that a Court of Appeals decision in the Seventh Circuit commented, "[t]aken literally, this definition would render almost all agreements executory since it is the rare agreement that does not involve unperformed obligations on either side."

Recognizing that a relaxed definition of "executory" would render nearly every contract "executory", the Court, following the Third Circuit, looked to the "Countryman" definition of an executory contract.

> "Professor Countryman defined an executory contract as 'a contract under which the obligation of both the bankrupt and the other party to the contract are so far underperformed that the failure of either to complete performance would constitute a material breach excusing performance of the other'. Further, '[t]he materiality of any remaining unperformed obligation is evaluated according to the relevant non-bankruptcy law'."

There was no argument that "closure of the club remained unperformed." Therefore, "[t]he dispute center[ed] upon whether [the municipality] had substantially performed its obligations under the [Settlement] Agreement at the time of the bankruptcy filing." That agreement provided that the club would close in exchange for the municipality's "designation of the Property as an area in need of redevelopment and adoption of an enhanced development plan for the Property so that the [club] could develop the property for high density residential uses."

The Court found the agreement to be "simple, straightforward and unambiguous on its face." Further, the Court found it "undisputed that by the end of 2003, [the municipality] had afforded [the go-go club] the extended two year period to operate its sexually-oriented business." It was also clear that the municipality had designated the property for "redevelopment and adopted a redevelopment plan." Consequently, the Court was convinced that the municipality "had substantially performed its obligations under the Agreement." To complete its analysis, the Court

looked at *Farnsworth on Contracts* 2nd edition Vol. 2, Part 3, Section 8.16. There it extracted the following: "The doctrine of material breach is simply the converse of the doctrine of substantial performance. . . . Substantial performance is performance without a material breach, and a material breach results in performance that is not substantial." Because the Court found that the municipality "did not have any substantial unperformed obligations under the Agreement at the time of the bankruptcy," it held that settlement agreement was not executory and therefore not subject to rejection. Accordingly, the Court denied the go-go club's bankruptcy motion to reject the agreement. It had no need to "address or make findings with respect" to whether the go-go club was acting in bad faith when seeking such a rejection "or whether rejection of the Agreement as an executory contract would somehow interfere with [the municipality's] enforcement of its 'police powers'."

BANKRUPTCY; HOMESTEAD; IMPAIRMENT; PREPAYMENT PENALTIES: A prepayment premium secured by a mortgage on the debtor's homestead should be considered when determining the amount of "all other liens on the property" for purposes of Sec. 522(f)(2)(A)(ii) of the Bankruptcy Code. ***In re Barrett, 2007 WL 1544658 (Bkrtcy D. Me. May 29, 2007)*** discussed under the heading: "Mortgages; Prepayment; Prepayment Penalties; Bankruptcy."

To demonstrate burden religious activities that government zoning officials must accommodate, applicant may simply demonstrate that alternative properties with property zoning are not available to it because it lacks adequate financial resources. ***Shepherd Montessori v. Anne Arbor Charter Township, 2007 WL 1486138 (Mich. App. 5/22/07)***, discussed under the heading: "Zoning and Land Use; Religious Activities; RLUIPA."

CONDOMINIUMS; ASSESSMENTS; MORTGAGEE IN POSSESSION: A mortgagee in possession of a condominium unit is personally liable for delinquent condominium common charges which accrue against the property's legal owner for services furnished during the mortgagee's possession and control of the premises. ***Woodview Condominium Association, Inc. v. Shanahan, 391 N.J. Super. 170, 917 A.2d 790 (App. Div. 2007)***, discussed under the heading: "Mortgages; Mortgagee in Possession; Common Fees."

CONDOMINIUMS; CONSTRUCTION DEFECTS: Condominium owners may assert a breach of contract claim against the building's developer for alleged defective design and construction even if the purchase agreement contains a limited warranty, so long as the cause of action arises from a separate contract provision. ***Tiffany at Westbury Condo v. Marelli Dev., 826 N.Y.S.2d 619 (A.D. 2 Dept. 2006).*** Plaintiffs brought suit against the condominium's developer for breach of contract due to alleged defects in the construction of the condominium. Although the purchase agreement contained a limited warranty and therefore precluded plaintiff's recovery based on common-law principles of implied warranty, the court found that plaintiffs might still assert a claim based on violations of specific provisions of the purchase agreement. The purchase agreement contained a provision whereby the condominium building, once erected, would be in substantial accordance with plans filed with the building department. In addition, the purchase agreement allowed the developer to substitute building materials, provided that they were of comparable value and quality as those set forth in the offering plan, which was attached to the purchase agreement. Because these provisions are independent of the limited warranty, the court held that the plaintiffs could assert a breach of contract claim against the developer.

CONDOMINIUMS; LIENS: Absent specific authority in the Declaration, a homeowner's association is not entitled to impose a lien on a homeowner's unit for unpaid fines. ***Walker v. Windsor Court Homeowners Ass'n*, 827 N.Y.S.2d (A.D. 2 Dept. 2006).** Plaintiff unit owner received notice of violations for which plaintiff failed to pay the associated fines. Due to plaintiff's failure to pay these fines, the development's homeowner's association placed a lien on the plaintiff's unit. Pursuant to the development's Declaration of Covenants, Restriction, Easements, Charges and Liens (the "Declaration"), the homeowner's association could impose a lien on property for unpaid assessments. "Assessment" was defined generally in the Declaration as a charge against real estate made to cover maintenance and operating expenses. Hence, the homeowner's association did not have the authority to impose a lien on plaintiff's unit for failure to pay fines.

CONSTITUTIONAL LAW; DUE PROCESS; NOTICE; TAX FORECLOSURE: Michigan Supreme Court invalidates statute that would have permitted tax

foreclosure authority to transfer irrevocable title to property in tax foreclosure even where authority had not provided notice to prior owner in accordance with statute or with Due Process. ***Wayne County Treasurer v. Perfecting Church, 2007 Westlaw 1518607 (5/23/07)***

The Michigan General Property Tax Act requires various forms of notice of imminent tax foreclosure to be provided to the owners of the property in foreclosure. Foreclosure in Michigan is carried out through a proceeding in the circuit court, in which the trial court rules upon the adequacy of the tax foreclosure procedure, including notice.

Upon judicial determination that the foreclosure is proper, the statute provides for a 21 day period to challenge the judgment of the foreclosing court. After that, the foreclosure is deemed final as to the title to the property. Any parties subsequently claiming that they did not receive notice in accordance with the statute are given a damages claim, but may not challenge the transfer of title.

In the instant case, it appears that the tax collection agency egregiously violated the notice requirements of the statute. Landowner had recently acquired two lots by one deed. It consulted the taxing authorities concerning tax liabilities, and the authorities erroneously told it about taxes relating to only one of the parcels, which landowner paid. The taxing authority informed the landowner that taxes were paid on both parcels, but soon thereafter the taxing authority proceeded to a tax foreclosure on the other parcel. Despite its prior discussion with the owner, and despite the recorded deed, the tax authorities sent notice only to the prior owner and did not post notice on the property, as the statute required.

The authority then proceeded to a judicial tax foreclosure and filed an affidavit indicating it had complied with the statute. As the affidavit was uncontested, the court ruled in favor of the foreclosure and the 21 days to challenge passed without the landowner ever knowing what was going on. The city forfeited the title and sold the property to investors.

The foreclosed landowner, which had acquired the property for parking for its adjacent church, was not interested in a damages remedy and brought suit to overturn the proceeding as without jurisdiction due to statutory and Constitutional notice defects.

The Michigan Supreme Court, affirming the judgment below, set aside the foreclosure on the grounds that the Michigan General Property Tax is unconstitutional, in that it in fact does provide that completion of the tax foreclosure proceeding vests unassailable title in the County, which the County can pass on to third party purchasers, even in cases where the County has blatantly and deliberately violated the notice requirements of the statute. The Court, consistent with the recent U.S. Supreme Court decision in *Jones v. Flowers, 547 U.S. 220, 126 S. Ct. 1708* (2006), noted that it is not Constitutionally required that a property owner receive *actual* notice of a public proceeding before property can be taken, but it is required that a Constitutionally sufficient effort be made to provide such notice. In this case, it was abundantly clear that no such effort had been made. Nevertheless, the statute would have granted final title to the County. Therefore, the court found, the statute was unconstitutional.

Comment 1: Note that *Jones* really doesn't require much of a foreclosing tax authority, and doesn't really say what is Constitutionally sufficient. But even the *Jones* court would have had no problem overturning the foreclosure in this case, since absolutely no effort had been made to notify the property owner.

Comment 2: But what about the 21 day appeals period? Apparently that is not the equivalent of a statute of limitations. There have been some decisions upholding relatively short limitations period for constitutional challenges, especially in the takings area. But it stands to reason that a short limitations period on a claim that a taking was invalid because of a failure of Constitutional notice ought not to be effective until the claimant has received adequate notice that a claim exists.

CONSTRUCTION; CLAIMS FOR DEFECTS; PRECLUSION BY LIMITED WARRANTY: Condominium owners may assert a breach of contract claim against the building's developer for alleged defective design and construction even if the purchase agreement contains a limited warranty, so long as the cause of action arises from a separate contract provision. ***Tiffany at Westbury Condo v. Marelli Dev., 826 N.Y.S.2d 619 (A.D. 2 Dept. 2006).*** Plaintiffs brought suit against the condominium's developer for breach of contract due to alleged defects in the construction of the condominium. Although the purchase agreement contained a limited warranty and therefore precluded plaintiff's recovery

based on common-law principles of implied warranty, the court found that plaintiffs might still assert a claim based on violations of specific provisions of the purchase agreement. The purchase agreement contained a provision whereby the condominium building, once erected, would be in substantial accordance with plans filed with the building department. In addition, the purchase agreement allowed the developer to substitute building materials, provided that they were of comparable value and quality as those set forth in the offering plan, which was attached to the purchase agreement. Because these provisions are independent of the limited warranty, the court held that the plaintiffs could assert a breach of contract claim against the developer.

CONSTRUCTION LAW; CONTRACTORS; INDEMNIFICATION: Although, at common law, a tortfeasor may be entitled to indemnification from another where the party's negligence is merely constructive, technical, imputed, or vicarious, in a case where liability arises from contract-based claims, an action for breach of contract is appropriate and an action for indemnification is not. ***Konover Construction Corporation v. East Coast Construction Services Corporation, 420 F. Supp.2d 366 (D. N.J. 2006); March 20, 2006.***

A general contractor hired a subcontractor to perform some work on a hotel under construction. Disputes arose between the contractor and the subcontractor and the subcontractor either withdrew or abandoned its work.

The subcontractor claimed it was entitled to attorneys' fees. The subcontract did not contain a fee-shifting provision. New Jersey Civil Practice Rules provide for fee shifting only in specific cases where the shifting is permitted by statute or the Civil Practice Rules. The Court found no such applicable rule in this case. In a contract dispute, without an express provision in a contract providing for fee-shifting, the general rule requires each party to pay its own counsel fees. Thus, the subcontractor's motion for summary judgment for attorneys' fees was dismissed. The subcontractor also sued the contractor for indemnification against claims made by the subcontractor's own sub-subcontractors. The Court found the subcontract did not require the contractor to indemnify the subcontractor. At common law, a tortfeasor may be entitled to indemnification from another where the party's negligence is merely constructive, technical, imputed or vicarious. In this case, the subcontractor's liability arose from contract-based claims brought by its own sub-subcontractors. According to the Court, if the subcontractor had a claim against the contractor, it would be for breach of contract, and not for indemnification. Thus, the sub-contractor's motion for summary judgment on its claim of indemnification was dismissed. The contractor sued claiming fraudulent and negligent misrepresentation. Both fraudulent and negligent misrepresentations require a claimant to sustain an injury caused by the other's misrepresentations. Under a theory of negligent misrepresentation, a claimant must prove the defendant negligently made an incorrect statement upon which the claimant relied, resulting in economic loss. To sustain a claim of fraudulent misrepresentation, a claimant must prove: (1) a material misrepresentation of fact; (2) knowledge or belief by the defendant of its falsity; (3) the defendant's intent that the plaintiff rely on the misstatement; (4) that the claimant did reasonably rely on the misstatement; and (5) resulting damages. Because the contractor offered no proof of damages, it could not sustain its motion for summary judgment on either its negligent or fraudulent misrepresentation claims.

COTENANCIES; PARTITION; JUDGMENT CREDITORS: Partition, an available remedy for a tenancy-in-common, is an equitable remedy and requires a balancing of the equities. ***Capital Finance Company of Delaware Valley, Inc. v. Asterbadi, 2006 WL 475318, (N.J. Super. Ch. Div. 2006); February 24, 2006.***

When a sheriff's sale deed to a husband and wife is silent as to the specific estate created in the property, a tenancy by the entirety is created. To create either a tenancy in common or a joint tenancy with the right of survivorship, the deed must explicitly state such intent. Partition is an equitable remedy, requiring the balancing of the equities of the co-tenants. However, in a tenancy by the entirety (which only exists between a husband and wife), each co-tenant possesses the right of survivorship, and partition is inequitable when it would destroy the right of survivorship.

In this case, a husband and wife acquired title to property through a sheriff's sale. The deed did not indicate that the transfer was to joint tenants with the right of survivorship, nor did it state that a tenancy in common was created, merely that title was vested in their two names. Consequently, they took title as tenants by the

entirety. In a tenancy by the entirety, both the husband and wife have a right of survivorship.

A judgment creditor subsequently purchased the husband's interest in the property at a second sheriff's sale. Because title to the property was held by the husband and wife as tenants by the entirety, the judgment creditor's acquisition of the husband's interest could not extinguish the wife's right of survivorship. Thus, the acquisition by the judgment creditor created a "tenancy in common with the right of survivorship."

Partition is an available remedy to a tenant in a tenancy in common. However, partition is an equitable remedy and requires a balancing of the equities of the co-tenants. Here, the property in question was a summer home, and the Court found there could be no real shared use of a summer home between the judgment creditor and the debtor's spouse. Consequently, the judgment creditor was deprived of all use and possession of the property. However, partition is not appropriate where, as here, it would destroy the debtor's spouse's right of survivorship. In balancing the equities, the Court found that the judgment creditor had other remedies that could be enforced. It ordered: (1) an accounting by the debtor's spouse; (2) that the judgment creditor and the debtor's spouse establish a fair rental value for the summer home which would form the basis of the debtor's spouse's obligation to the judgment creditor; and (3) that the judgment creditor had to offset this obligation by its own share of costs and taxes associated with the property.

EASEMENTS; CREATION; DEDICATION; PUBLIC DEDICATION: When lands are sold with reference to a map upon which appear a dedication of certain areas to the public as a park, but there is no immediate acceptance of such dedication, this establishes an offer of dedication that cannot be revoked except by consent of the municipality; therefore, when the affected property is sold, even in a tax sale, it is sold subject to the municipality's right to accept the dedication. ***Township of Middletown v. Simon, 387 N.J. Super. 65, 903 A.2d 418 (App. Div. 2006); July 31, 2006.***, discussed under the heading: "Municipal Law; Dedication; Acceptance; Parks."

EMINENT DOMAIN; COMPENSABLE INTERESTS; LACK OF ACCESS: A property owner is not entitled to consequential damages for lack of legal access resulting from the State's condemnation of private land to improve an abutting highway if the state implicitly reestablishes access through permanent easements. ***Lake George Associates v. State of New York, 824 N.Y.S.2d 196 (Ct. App. 2006)***. The State appropriated land from a shopping center owned by Lake George Associates in order to create turn lanes on two state highways. As a result of the appropriation, the shopping center did not have complete direct access to both lanes of the highways. Instead access was possible only through a driveway on a neighboring landowner's property. The court found that although a landowner is entitled to consequential damages if it is denied legal access to its property through an appropriation, sufficient access does not need to be established through a formal conveyance to the landowner. In implementing the appropriation, the State reserved permanent easements in the neighboring landowner's property in order to establish access to public roads through the use of joint driveways. Although the easements on their face did not permit cross-vehicular access rights, the court found that an implicit legal right of access was created because of the mandate of Highway Law '10 that empowers the Commissioner of Transportation to obtain land in order to reestablish access to public roads.

EMINENT DOMAIN; PROCEDURE; NOTICE: Where a condemning authority easily could obtain the property owner's address from its own records, that authority violates statutory requirements and denies the property owner of constitutional due process if it fails to serve a condemnation notice, making it mandatory that the condemnation procedure begin anew even if the statute of limitations has already expired. ***City of Passaic v. Shennett, 390 N.J. Super. 475, 915 A.2d 1092 (App. Div. 2007)***

An individual was conveyed land by a family member. The land had been in the family for over fifty years. After the conveyance, a house situated on the land burned down and the lot remained vacant. The individual continued to pay property taxes for nearly two decades. Thereafter, the municipality instituted a condemnation action alleging that the land had been abandoned. Significantly, the taxes on the land were fully paid. Nonetheless, the municipality mailed a notice to the individual, which was returned for omitting the individual's apartment designation. The municipality also publicized the condemnation proceeding in the local newspaper. After proceeding unopposed, the municipality was successful in procuring an order from the lower court authorizing it to acquire the

property, appointing commissioners to appraise the land, and fixing compensation for the taking pursuant to eminent domain. The municipality deposited the requisite sum with the court and took title to the property.

Subsequently, the municipality sold the property to an asset management company. When the individual did not receive a property tax statement, he discovered that the property had been condemned, sold, and that the asset management company had already erected a new home. The individual moved to vacate the condemnation and valuation orders, citing lack of service of process, erroneous findings of abandonment, undervaluation of the property, and lack of notice of the commissioner's hearings. The lower court noted that the municipality never attempted to personally serve the individual with proper notice; still, because the property had already been sold and construction had begun, the lower court refused to vacate the judgment. The lower court did, however, grant the individual's motion to vacate the valuation order. Then, a hearing was held, the individual was given notice, and the property was valued at a significantly higher figure.

The individual appealed the lower court's refusal to vacate its initial order of condemnation and the Appellate Division reversed, holding that the proper service is a prerequisite to a condemnation complaint under state law. Furthermore, under state law, the municipality was required to engage in *bona fide* negotiations with the prospective condemnee unless the condemnee is unknown, out of state, or for other good cause shown. Since the municipality could have easily obtained the individual's address from its own tax rolls, the municipality violated the statutory requirements. Moreover, the Court pointed out that the notice requirement was jurisdictional. Federal constitutional due process requires that a default judgment be vacated when lack of jurisdiction is apparent, and thus the lower court's decision to revisit only the question of valuation was an inadequate remedy. It followed that the lower court's judgment was void and could be vacated, the statute of limitations notwithstanding.

Thus, the lower court's denial of the individual's motion to vacate the judgment of condemnation was reversed and remanded for further consideration.

Comment: Readers should compare recent decisions involving Due Process claims in the tax foreclosure area. They are not nearly so favorable toward the victims of municipal sloppiness: *Jones v. Flowers, 547 U.S. _____, 2006 Westlaw 1082955 (4/24/06)* (The DIRT DD for 4/27/06) (Supreme Court reinterprets *Mullane* in context of tax foreclosures. County collector must do "something" when it becomes aware that its mailed notice of foreclosure has not been delivered to the property owner. But Court mum on exactly what that "something" is.); *Mosssafa v. Kleiman, 2003 WL 443797 (N.Y. 2/25/03)* (The DIRT DD for 4/4/03) In *Mossafa*, the New York Court of Appeals held that the local tax collector had no duty to seek out the taxpayer's actual address even when a letter was returned with the legend that the taxpayer was not at the notice address and had not received the notice. The New York court did acknowledge that the tax collector could not simply ignore the fact that it knew that the notice had not been received, but that its further duty was limited to simply looking in the surrogate's office for an alternate address. It had no duty to look in other county records, such as voting rolls. The editor found that result "shocking" and inconsistent with his view of *Mullane*.

EMINENT DOMAIN; URBAN RENEWAL; "BLIGHT": A determination of blight for purposes of a condemnation by a redevelopment corporation in Missouri must be based on evidence of both economic and social liabilities in the project area; economic liabilities alone are not sufficient. ***Centene Plaza Redevelopment Corp. V. Mnt Properties, 2007 WL 1695153 (June 12, 2007).***

Under Mo. Rev. Stat. ch. 353, a city government may authorize a privately owned redevelopment corporation to take land for redevelopment purposes upon a showing that the land contains "blight". In response to the city government's RFP, Centene Redevelopment Corporation decided to redevelop a block in Clayton, Missouri. Clayton is the "new downtown" of the St. Louis metropolitan area, characterized by many modern high rise office buildings, hotels, and the like. Centene was able to acquire most of the properties on the block by negotiated purchase, but Mint Properties, the owner of two office buildings on the block, refused to sell. The buildings in question were relatively lowrise, somewhat older, and might be considered an underutilization of this very valuable real estate.

The city's consultant determined that the block was blighted, and the city passed an ordinance so declaring.

Centene then filed suit to condemn the two remaining buildings. Mint Properties appealed the condemnation order on the ground that the statutory definition of blight was not satisfied. The Missouri Supreme Court agreed.

The Missouri statute's definition of blight is fairly typical. It provides that a blighted area consists of those portions of the city that "by reason of age, obsolescence, inadequate or outmoded design or physical deterioration have become economic and social liabilities, and that such conditions are conducive to ill health, transmission of disease, crime or inability to pay reasonable taxes."

The court found that several of the statutory factors were present. The buildings were old, somewhat obsolete, and did not return much in the way of tax revenues to the city. However, the court focused on the phrase "economic and social liabilities", with emphasis on "and". The liabilities in this case were purely economic, the court found. There was no evidence at all to support the presence of "social liabilities".

Specifically, there was no evidence of high crime, vandalism, fire risk, or public health problems. While the city had expressed concern over some of these problems, the court found that there was literally no evidence at all that they actually existed. While the blight determination can, under Missouri law, encompass individual nblighted properties in the redevelopment area, this did not help the city, since "there is a lack of evidence of social liability as to any portion of the area sought to be condemned."

Following the statute literally, the court concluded that both economic and social liabilities had to exist in order to warrant a blight determination. In the complete absence of social liabilities, the court reversed the city's finding of blight and the order of condemnation.

Reporter's Comment 1: Note carefully that this is not a constitutional decision. The court expressly points out that it is making no determination as to whether there is a "public use" sufficient to justify condemnation. Hence, this decision can't be regarded as literally anti-Kelo Nonetheless, its practical thrust is obviously to make condemnations for economic development purposes more difficult, since a social need for the redevelopment must also be shown. The Missouri legislature in 2006 enacted an amendment to the state's condemnation statute prohibiting takings "solely for economic development purposes".

Reporter's Comment 2: In the past fifty years, the Missouri appellate courts have virtually never reversed a city's determination of blight. The courts have always employed an extremely lenient standard in reviewing cities' actions: that determination of blight must not be arbitrary or induced by fraud, collusion or bad faith. Here, the court evidently determined that the city's decision was indeed arbitrary, being based on no evidence whatever. The present case seems to evince at least a slightly stronger interest on the part of the court in reviewing city blight determinations.

Reporter's Comment 3: A 2006 amendment to the statute added a requirement that a legislative determination of blight also must be supported by substantial evidence. I had previously opined that this really added nothing and did not change the standard of judicial review; see Whitman, Eminent Domain Reform in Missouri: A Legislative Memoir, 71 Mo.L.Rev. 721 (2006). The court seems to have agreed; it held that it was unnecessary to determine whether the amendment applied retroactively, since the city's determination did not meet either the old or the new standard.

Reporter's Comment 4: It remains to be seen what the court will do when faced with a case in which there is some, but not very much, evidence of "social liability". Taken at face value, this opinion seems to indicate that the court will acquiesce in the city's determination.

Reporter's Comment 5: The statute before the court in this case is not the only redevelopment statute in Missouri; there are two others. Under Mo. Rev. Stat. § 99.300 et seq., it is the city's redevelopment authority, rather than a private redevelopment corporation like Centene, that engages in the redevelopment activity. The definition of blight is different in 99.300: "'Blighted" shall mean any area where dwellings predominate which, by reason of dilapidation, overcrowding, lack of ventilation, light or sanitary facilities or any combination of these factors are detrimental to safety, health and morals."

This statute also uses the conjunctive: "safety, health and morals". Perhaps the court would read it in a manner similar to its interpretation of Ch. 353, and require that all three of those issues, safety, health, and morals, be at risk in the project area. But in any event, 99.300 et. seq. couldn't have been used at all in the *Centene* case, even if the city had wanted to become the redeveloper, because 99.300 requires that dwellings predominate in the project

area. I believe that the area to be covered by the Centene project didn't have any dwellings in it at all; it was entirely commercial.

The third statute, Mo. Rev. Stat. § 99.800 et. seq., is for use in tax increment financing (TIF) projects, and the city's TIF authority must exercise the eminent domain power. (See Mo Rev. Stat. § 99.460.) TIF has been widely used in redevelopment projects, especially in the St. Louis metropolitan area. Certainly the city of Clayton might have made the Centene project a TIF project, although in fact it apparently did not.

The blight definition in the TIF statute is, once again, different. The statute lists some of the same factors as in Ch. 353, discussed above, and then provides that blight exists if one or more of these factors "retards the provision of housing accommodations or constitutes an economic or social liability or a menace to the public health, safety, morals, or welfare in its present condition and use." The phrase used here is "economic or social liability" in the disjunctive, not the conjunctive "economic and social liability" of Ch. 353. Moreover, that "liability" provides just one of three possible justifications for a finding of blight, the other two being the retarding of provision of housing and the menacing of the public health, safety, morals or welfare.

This standard in 99.800 et. seq. is obviously much more lenient than either of the other two redevelopment statutes. It would therefore not be surprising to see an upswing in the use of TIF financing and in condemnation by TIF authorities in future cases in which the project area is primarily or exclusively nonresidential property.

Reporter's Comment 6: The case illustrates that the exact statutory definition can matter a great deal. I must confess that, while I have read all three of the Missouri statutory blight definitions many times, I had never focused carefully on the differences among them. In fact, my eyes tended to glaze over when I read the "boilerplate". I think I'll have to be more careful in the future.

Editor's Comment: Also see . ***Gallenthin Realty Development, Inc. v. Borough of Paulsboro, 2007 WL 1687274 (N.J. Supr. Ct. 2007 6/13/07),*** discussed under the heading: "Zoning and Land Use; Redevelopment; Blight." (The New Jersey Constitution does not permit government redevelopment of private property solely because the property is not used in an optimal manner.)

The Reporter for this item was Professor Dale Whitman at the University of Missouri, Columbia.

FAIR DEBT COLLECTION; FORECLOSURE: Under the Fair Debt Collection Practices Act, a debt collector (which includes an attorney regularly engaged in debt collection activity), need only include, in its initial communication to a borrower, notice that it is attempting to collect a debt and that any information obtained would be used for that purpose; and once that notice has been given, it is not necessary to include the notice within subsequent communications. A foreclosure Complaint may be the "first communication." ***Barrows v. Chase Manhattan Mortgage Corporation, 2006 WL 3626883 (U.S. Dist. Ct. D. N.J. 2006) 12/06/06)***

A borrower fell behind on her mortgage payments and her lender, through retained counsel, filed a foreclosure complaint. Counsel then sent a letter to the borrower setting forth the amount necessary to clear the debt, including the figure of $2,500 for attorney's fees.

The borrower responded with a lawsuit against the lender's lawyers claiming that they had violated the Fair Debt Collection Practices Act (FDCPA) when they overstated in the letter the sum required to reinstate her loan. The suit was styled as a class action, but this opinion does not say much about the class action aspects of the suit.

The attorneys claimed that the borrower's suit should be dismissed because they were not debt collectors and because the borrower, in eventually selling her house and paying off the mortgage, never paid those attorneys' fees. They argued that the letter simply was stating the amount necessary to clear the default (as to which a foreclosure suit had been filed.)

The Court disagreed, noting that attorneys are not excluded from the FDCPA definition of "debt collectors" if they regularly engage in debt collection activity. The Court also found that under the FDCPA, a debt collector is prohibited from using "unfair or unconscionable means to collect or attempt to collect" a debt. Therefore, if the attorneys were found to have attempted to collect fees that are determined to be in excess of those allowed under state law, they could be found to have violated the FDCPA even if they never collected those fees. An FDCPA violation is punishable by a damages award not to exceed $1,000 in addition to actual damages.

The borrower also claimed that the attorneys violated the FDCPA by failing to include in the letter the "mini-Miranda" warning required under the statute. Under the FDCPA, a debt collector must include, in its initial communication to the borrower, a notice that it is attempting to collect a debt that any information obtained will be used for that purpose. In subsequent communications, the mini-Miranda warning is not required as long as the debt collector identifies itself as such. The Court found that the foreclosure complaint contained the necessary warnings, so that the subsequent letter to the borrower did not need to contain the warning. The Court also found that the attorneys did not need to specifically identify themselves in the letter as debt collectors, as long as the letter was clearly and directly related to the foreclosure action.

Substantively, the court gave a hint as to how the attorney's fee issue was going to turn out. Although the complaint survived summary judgment, the court noted that the note and mortgage did permit attorney's fees, but that such fees were subject to limits under New Jersey law, which establishes a sliding scale for permitted fees based upon the amount in dispute. We're not told the amount in dispute, but under the bit of the scale the court set forth, it is quite likely that most foreclosure would support a fee claim of $2,500. The court didn't seem troubled with the fact that the fees were demanded immediately upon filing of the claim, perhaps because that is permitted by the statute.

There were a number of rulings on New Jersey consumer law issues that are not discussed here.

Comment: The FDCPA is a technical and treacherous piece of legislation that has far broader reach than most lawyers seem to realize. The definition of "debt collector" is quite broad, and probably applies to most lawyers with consumer lender clients, and to most lawyers doing evictions in residential real estate, even if someone else is doing the actual foreclosures and collection actions. The preliminary demand letters may be all that is necessary to catch you up in the net.

Once one is a "debt collector", one must conform one's practice to the technical requirements of the Act, which include required notices, cure periods (that might not apply to the creditor itself if it collects) and restrictions on communications with non-debtor parties. A periodic FDCPA systems audit probably is in order to insure that there is full compliance. Except for the danger of class actions, the liabilities under the Act aren't all that scary, but failure to comply occasionally can mess up the position of your client creditor and of course can embarrass the client's less than careful lawyer.

FIXTURES; FLOATING DOCKS: Floating docks are not real property within the meaning of casualty insurance policy. ***American Home Assurance Co. v. AGM Marine Contractors, Inc., 467 F.3d. 810 (1st Cir. 2006),*** discussed under the heading: "Wharfs and Docks; 'Property'."

HOMESTEAD; IMPAIRMENT; PREPAYMENT PENALTIES: A prepayment premium secured by a mortgage on the debtor's homestead should be considered when determining the amount of "all other liens on the property" for purposes of Sec. 522(f)(2)(A)(ii) of the Bankruptcy Code. ***In re Barrett, 2007 WL 1544658 (Bkrtcy D. Me. May 29, 2007)*** discussed under the heading: "Mortgages; Prepayment; Prepayment Penalties; Bankruptcy."

INSURANCE; HOMEOWNER'S INSURANCE; POLICY LIMITS: Under a standard Homeowners Form B policy, an insurer is not liable to its insured for multiple losses sustained during a policy period for an amount in excess of its limit of liability. ***Coats v. Farmers Ins., 14-04-00686-CV (Tex. App. 2006)***.

In this case of first impression, Farmers issued a homeowner's policy to the Coats which was effective from July 30, 2000 to July 31, 2001. In June 2001, the Coats filed a claim for water and roof damage to their home caused by Tropical Storm Allison. During March 2002, Farmers declared that the Coats' residence was a total loss and paid the policy limits for the dwelling and for loss of use including alternative living expenses.

In July 2002, the Coats filed another claim alleging an HVAC overflow had caused water and mold damage to the dwelling. Farmers investigated and determined the alleged damage was considered when the Coats received their previous payment under the policy.

In December 2002, the Coats filed suit against Farmers for nonpayment of the subsequent HVAC claim and violations of the Texas Insurance Code, which requires an insurer to submit payment to an insured within sixty days (unless otherwise specified by applicable statute) of a proven loss.

The trial court granted Farmers' motion for summary judgment due to the fact that Farmers had already paid the Coats the policy limits.

On appeal, the Court of Appeals affirmed the trial court's decision with respect to Farmers contractual liability under the homeowner's policy. The court rejected the Coats' argument that the standard Homeowners Form B, which is prescribed by the Texas Department of Insurance, is ambiguous or requires Farmers to remit an amount not to exceed the policy limits for each loss sustained during the policy period. The policy states that Farmers "will not be liable in *any one loss*Yfor more than the applicable limit of liability" (emphasis added).

The Coats pointed to authority from another state that held that the phrase at issue creates an ambiguity because there was no specific language limiting payment to the declared policy limit regardless of the number of claims filed during the policy period. The court here, however, stated that when read as a whole, the policy is not ambiguous. The court reasoned that the phrase "any one loss" only requires Farmers to pay an amount not to exceed the policy limits to be allocated between two or more multiple insureds as their interests appear. In support of this notion, it points to the language of another provision which provides that Farmers payment under the policy "will not exceedYthe limit of liability under this policy applicable to the damaged or destroyed building structure(s)." The court did, however, reverse that portion of the trial court's order granting summary judgment in favor of Farmers on the Coats' claim under the Texas Insurance Code due to Farmers' failure to present conclusive proof refuting this claim.

LANDLORD/TENANT; HOLDOVER; LANDLORD'S REMEDIES: Court upholds lease provision socking tenant with double rent for period of holding over. ***Brunswick Limited P'tnshp v. Feudo, 2007 Westlaw 1310260 (Ohio App. 5/4/2007),*** reported under the heading: "Landlord/Tenant; Landlord's Remedies; Holdover."

What makes this case particularly interesting is that it distinguishes another Ohio case, *Village Station v. Geauga*, 616 N.E. 2d 1201 (Ohio App. 1992) that held that a double rent clause was unconscionable and unenforceable when it provided for double rent when tenant became bound to a new month to month lease on holdover but didn't stay for a full month.

Here the lease provided that if the tenant held over, no new lease would result, and the tenant would be regarded as a trespasser, subject to immediate eviction, and the landlord had the right to charge the tenant double rent for the period of holdover. The tenant held over for four months, paying the same rent that it had paid under the original five year lease. The landlord, of course, cashed the checks. But, when the tenant vacated, the landlord sought the additional double rent. The court upheld an award for double rent plus expense pass through additional rent (as also provided in the lease) and attorney's fees.

The court noted that other courts had upheld double and even triple rent provisions where the parties knowingly agreed to them in a commercial lease, citing cases in D.C. and Georgia.

Comment 1: It is true that if the landlord and tenant stipulate that a new lease will result from holding over, with a new rental, this amounts to no more than a new lease agreement and certainly is enforceable. What makes this case a bit different is the express statement that there is no new lease agreement and the tenant is strictly a trespasser. Thus the provision is clearly a liquidate damages clause, and a stipulation that a reasonable liquidated damages is double rent.

Comment 2: The precedent case, *Village Station,* contained an extremely ambiguous holdover clause that said in one breath that no new lease arose and that the tenant was one "at will and at sufferance" but then later that the tenant was bound on a month to month basis. So the landlord, which could arguably have put into the lease that a new month to month lease at a double rental would apply, apparently did not want to be bound even to one rent period of holdover, but wanted the tenant bound to one rent period as damages.

The current case properly differentiates *Village Station*, but still is vulnerable to the criticism that double rent is a pretty high figure for liquidated damages. Norm Guttmacher, the Ohio lawyer who sent the case in, commented: "I have rarely come across a case where a court specifically holds that, in a commercial lease situation, a 'double rent' provision for a holdover tenant is enforceable and is neither unconscionable nor unenforceable as a penalty. I'm not sure how often this issue is squarely faced by courts; but given the prevalence of this type of provision in commercial leases, it is reassuring at least to counsel for landlords."

Comment 3: In fact, where the courts see knowledgeable commercial parties agreeing to a specific estimate of damages, they frequently will hold the parties to their bargain, and won't take a second look. *Village Station* was the exception because of the obvious disproportionality in the formula itself.

Comment 4: For an interesting comparison case, applying a generous liquidated damages analysis to a tenant remedy provision, see: *Bates Adver. USA, Inc. v. 498 Seventh, LLC,* 850 N.E.2d 1137 (N.Y. 2006). (the DIRT DD for 11/4/06) (A lease provision entitling a tenant to rent abatement if the landlord fails to complete safety and security improvements as specified is a permissible liquidated damages provision and not a penalty unless the challenging party shows that tenant's actual damages were readily ascertainable at the time of contract or that the provision entitles tenant to a benefit grossly disproportionate to its actual damages.)

LANDLORD/TENANT; OPTIONS TO PURCHASE: Tenant's option to purchase "marketable fee simple title" entitles tenant to acquire property free of below market leases entered into by landlord prior to tenant's exercise of the option. ***Van Carr Enter. v. Hamco, Inc.,2006 WL 649985 (Ark. 3/15/06)***

This case is discussed further under the heading: "Specific Performance; Usurious Interest Rate."

Landlord and tenant entered into a fixed term commercial lease agreement with an option to purchase the building, which could be exercised at any time during the period of the lease. The option provided that "conveyance of the Property shall be made to Buyer by general warranty deed, in fee simple absolute, except it shall be subject to recorded instrument and easements if any, which do not materially affect the value of the Property."

During the term of tenant's lease, landlord entered into two separate leases with a subsidiary of landlord for two different suites in the building, both at below market rent. Four months prior to the expiration of tenant's lease, tenant gave written notice to landlord of tenant's intent to exercise its option to purchase. The landlord tried to avoid the option on a number of grounds, discussed in part under the other discussion noted above. It also insisted that tenant take the property subject to existing leases.

Ultimately, the trial court granted specific performance to the tenant free and clear of the leases.

On landlord's appeal, the appeals court upheld the trial court. The Arkansas court dealt with the problem as one of marketable title. It stated that the option agreement implicitly required the landlord to deliver marketable title, and held that, since the leases were clearly below market and renewable at "shockingly low renewal prices" they affected marketability.

Comment 1: Why go through this analysis? Don't all leases render title unmarketable unless the purchaser agrees to accept them? Don't they affect the buyer's right to possess the property?

Comment 2: One might also surmise that a lessee taking with knowledge of the optionee's rights takes subject to the option. Unfortunately, the cases aren't uniform on this point. There are cases collected in Friedman on Leases, Randolph edition, at section 15:5:1, that go both ways, depending upon whether a court regards an option as a real estate interest and/or whether it views the optionee's rights are "relating back" to the creation of the option.

The "marketability" inference clearly has not been convincing to many courts considering these cases.

Compare: Wachovia Bank v. Lifetime Industries, Inc., 145 Cal. App. 4th 1039, 32 Cal. Rptr. 3d 168 (Cal. App. 2006) Where real property is subject to a recorded option interest, any party subsequently obtaining an interest in the optioned property obtains that interest subject to the option rights. Nevertheless, such party's rights are valid against the title of the original optionor prior to transfer of title pursuant to the option, even though the optionee has given notice of exercise of the option.

LANDLORD/TENANT; OPTIONS TO PURCHASE; EXERCISE: Where purchaser deposits substantial cash payment at outset of lease option period, and purchaser's "rent" thereafter corresponds closely to the varying payments on seller's underlying mortgage, purchaser may be viewed as having already exercised option, even though he dies nine years later without having formally exercised the option. ***Lee v. Bass, 2007 Westlaw 505386 (2/20/07) (opinion not yet finally approved for publication)***, discussed under the heading: "Vendor/purchaser; Lease Option; Exercise."

LANDLORD/TENANT; RESIDENTIAL; ANTI-EVICTION STATUTE: Under New Jersey anti-eviction statute, where a landlord has asserted the right to evict a residential tenant because the landlord intends to personally occupy the unit, it is the landlord who has the burden to show that its subsequent failure to occupy the apartment was not arbitrary and that the reason for eviction was not pretextual. ***Hale v. Farrakhan, 390 N.J. Super. 335, 915 A.2d 581 (App. Div. 2007)***

LANDLORD/TENANT; WAIVERS OF NEGLIGENCE: An indemnification clause in a commercial lease that requires a tenant to indemnify a landlord for its own negligence is enforceable when the purpose of the provision is to allocate risk of loss among third party insurance carriers. ***Great Northern Insurance Company v. Interior Construction Corp., 823 N.Y.S.2d 765 (Ct. App. 2006)***. A tenant in a commercial office building renovated its premises and during the course of renovations flooded another tenant's premises. The parties stipulated that the tenant was 10% at fault and that the landlord was 90% at fault for the flood. The tenant's lease contained an indemnification provision whereby the tenant would indemnify the landlord for any accident occurring at the premises, unless the accident was caused solely by the landlord's negligence. Importantly, the tenant's lease also contained an insurance procurement requirement, mandating that the tenant obtain general liability insurance coverage and name the landlord as an additional insured party. The landlord invoked this indemnification provision when the flooded tenant's insurance carrier sued the landlord for damages. An indemnification provision which indemnifies a party for its own negligence is only enforceable if it was the "unmistakable intent" of the parties was to create such an obligation. The Court found that this intent existed based on the plain language of the indemnification provision. The Court held that such a provision is not against public policy because the purpose of the provision is not to exempt the landlord from liability but to allocate risk of loss among third party insurance carriers.

LANDLORD/TENANT; WASTE: It is waste for a long term tenant to sublease to the City a right to build a retention pond on the land, necessitating the removal of four feet of soil, where the City intends that the retention pond will be a permanent installation, when the City could acquire the property now by eminent domain. ***Hood v. Freemon, 2007 Westlaw 27121 (Tenn. App. 1/3/07) (unreported case)***

This case is of some note because the victorious counsel, obtaining reversal on appeal, is DIRTer H. Anthony Duncan of Franklin, Tennessee.

Landlord leased a 6-acre parcel to tenant for an initial ten-year term with renewals at lessee's option for successive ten year terms not to exceed 99 years. The rent was $300 per month (plus taxes) for the first 20 years, rising to $500 per month thereafter. Although 80% of the land was "swampy", there was a portion along the highway that proved valuable to tenant. He subleased to various users to generate a return of $4,000 to $5,000 a month.

Obviously, the lease in general was beneficial to the tenant's side, but there was a provision that stated that in the event of eminent domain, the landlord would receive all compensation for the land while tenant would be compensated only for the value of any buildings tenant had constructed.

The local city wished to add the land to a larger retention pond it was intending to build. It approach Tenant for the rights to do so, but, upon discovering the circumstances of the lease arrangement, went to Landlord and proposed to pay Landlord a portion of the fair market value of the property, with the rest going to Tenant. Landlord balked at this, because, under the lease, the Landlord would get all the proceeds if the City had condemned the property, since the City planned to leave the valuable commercial sublease property intact.

Tenant then proposed to sublease the land to City. City, in order to insure that the lease remained in place, would pay all the ground rent and the taxes directly to Landlord. Presumably there was some "kicker" to Tenant. Otherwise, Tenant could have simply waived any claim to compensation and let city acquire the land.

City admitted that it believed that the retention pond would be permanent and that, if and when the lease ended, City would likely acquire Landlord's interest by eminent domain.

The consequence of the deal, of course, was that "the rich got richer" in that Tenant would reap all the benefits of the value of the retention pond for the balance of the term, even though the City could have used eminent domain to terminate his lease and acquire the land, in which case Landlord would have received nothing.

The landlord sought to enjoin the proposed project as waste. The trial court found no waste and denied the injunction, commenting that in any event landlord had an adequate remedy in damages. The appeals court here reversed, finding that the proposed project did constitute waste by the tenant and remanding for determination as to whether the landlord's legal remedies were sufficient to justify denying the injunction.

The court noted that a significant change in the character of the land that could have an adverse impact on its value in the hands of the landlord constituted tenant waste. The court stated that it was "axiomatic" that removing four feet of dirt from the land and building a permanent retention pond there would "both damage the remainder and have and diminish the value of the property." Hence, it was an easy determination that waste would occur.

The court also noted that on remand the court could consider whether the proposed waste would constitute breach of the lease. (We are not told whether the lease provided with a remedy of termination for waste, or even whether waste was itemized as a breach).

Comment 1: This is a cute little case, and indicates the problems that arise in measuring the rights of parties under a long term ground lease. Better for them to try to be more specific in anticipating what changes the landlord is prepared to permit, because certainly over a 100 year term the tenant is going to have lots of novel ideas.

Comment 2: On what point in time does a court focus in reaching a determination of whether certain changes in the land would constitute waste? At the time they are made, even though the tenant retains possession? At lease end only? Shouldn't the landlord be protected in the event that the tenant abandons or otherwise terminates the lease prematurely? The editor believes that the court should consider whether the change, at the time of the court's judgment, is a change that adversely affects the value. Then it should determine whether the parties, expressly or implicitly, intended that the tenant have the right to implement this kind of change. If not, it's waste.

LANDOWNER LIABILITY; SIDEWALKS; MUNICIPALITIES: For a municipality to be liable for a person injured by a sidewalk defect caused by tree roots, that individual would need to prove that the municipality prohibited the adjacent property owner from trimming the tree, that the prohibition caused the sidewalk to lift and become dangerous, and that the condition of the sidewalk created a foreseeable risk that a pedestrian would trip and suffer injuries. ***Roman v. City of North Plainfield, 388 N.J. Super. 527, 909 A.2d 760 (App. Div. 2006); November 6, 2006.***

A woman was injured when she tripped on an upraised sidewalk abutting commercial property. The woman sued the property owner and the municipality. After the woman presented her evidence, the municipality moved for an involuntary dismissal of the complaint. The municipality argued that, under the Tort Claims Act, it was not liable for injuries caused on property that it did not own or control. The lower court agreed and dismissed the complaint. The woman appealed, and the Appellate Division reversed. It found that the matter should have been tried by a jury. It noted that, on a motion to dismiss, the nonmoving party is to be given every favorable inference. If, after giving all favorable inferences to the nonmoving party, there is insufficient evidence, then the case may be dismissed. In this case, the commercial property owner testified that he had known about the upraised sidewalk slabs for many years and that the municipality became aware of the problem during its inspections over the years. He also testified that he contacted the municipality, since he would have been required to cut the tree roots of the municipality owned tree in order to correct the problem. He also testified that he did not receive permission to cut the tree and assumed the municipality was going to cut the tree roots. His testimony was contradicted by a municipal employee who testified having no record of any conversations regarding the tree.

The lower court had concluded that the municipality had no control over the sidewalk, and was therefore immune from liability for injuries sustained by the woman when she tripped, but the Appellate Division disagreed. Without determining whether or not the municipality was liable for the injuries, the Court found that the woman presented sufficient evidence to claim that, by dictating whether or not the tree roots could be trimmed, the municipality exercised control over the sidewalk. The Court noted that in order to prevail, the woman still needed to demonstrate that the municipality was negligent with respect to maintenance of the sidewalk. She needed to prove that municipality prohibited the owner from trimming the tree, that the prohibition caused the sidewalk to lift and become dangerous, and that the condition of the sidewalk

created a foreseeable risk that a pedestrian would trip and suffer injuries.

LANDOWNER LIABILITY; SIDEWALKS; MUNICIPALITIES: Where a shade tree commission's powers are limited to making recommendations to its municipality, it is the municipality that may be liable for a defective sidewalk condition if the municipality knew of the dangerous condition or had constructive knowledge of its condition and failed to make appropriate repairs. ***Lodato v. Evesham Township, 388 N.J. Super. 501, 909 A.2d 745 (App. Div. 2006); November 1, 2006.***

Roots from a tree located between the street and the sidewalk raised the sidewalk in front of a certain homeowner's house by four inches. That was the sidewalk's condition for all of the eighteen years that the owner owned the property, as the tree had been planted by the property's developer. According to the owner, most of the houses on that block had raised sidewalks, and the neighbors on both sides of his house had the municipality remove the shade trees in order to repair the sidewalks in front of their houses. The owner never notified the municipality regarding the condition of the sidewalk. If a complaint had been made, it would have gone to the municipality's Department of Public Works, which could remove the tree at its own discretion. The municipality had created a shade tree advisory commission to make recommendations as to what type of trees to plant and where to plant them.

A neighbor who had previously never traveled on that particular sidewalk was walking by when the raised sidewalk caused him to fall and break his ankle. He brought a personal injury suit against the homeowner, the shade tree advisory commission, and the municipality. The lower court granted the owner's motion for summary judgment, finding that he had no common law duty to maintain the sidewalk in front of his house. It also granted summary judgment in favor of the commission and the municipality, finding that there was no actual or constructive knowledge to establish a *prima facie* case against them. The neighbor's motion for reconsideration was denied.

On appeal, the Appellate Division affirmed the grant of summary judgment in favor of the owner and the commission. It reversed the order granting summary judgment to the municipality and remanded the case for trial, finding that the injured neighbor presented sufficient proofs to create a question of fact as to whether the municipality had constructive notice of the raised sidewalk. With regard to the homeowner, the neighbor argued that the owner should have been held liable for failure to repair the sidewalk because he was obligated under the municipality's ordinances to maintain the sidewalk. The Court found that the lower court was correct in finding that homeowners are protected by common law public sidewalk immunity. It explained that municipal ordinances do not create a tort duty. Therefore, the owner was entitled to summary judgment.

Regarding the shade tree commission, the Court discussed the differences between a statutory and an advisory commission. Unlike a statutory commission, an advisory commission like the one in the present case has no power, control or appropriation. While a statutory shade tree commission could require that any tree posing a safety hazard be removed, the advisory commission's power was limited to making recommendations at the municipality's request. Therefore, in the present case where the commission was advisory, the power to act remained with the municipality. As the record disclosed no proof that the commission had any power to control tree removal, and the municipality never put the commission in a position to acquire knowledge of any dangerous condition, the Court found that summary judgment was appropriate.

With respect to the claim against the municipality, the Court noted that the neighbor would prevail if he established that the municipality had actual or constructive notice of the dangerous condition. While the municipality did not receive actual notice of the raised sidewalk, the Court found that the question remained whether the injured neighbor presented sufficient proofs to demonstrate constructive knowledge. If he showed that the dangerous condition existed for so long or was so obvious that the municipality should have discovered it, the neighbor would prevail on his claim. The Court found that the tree roots and raised sidewalk condition was open and obvious. The evidence also established that the condition had existed for eighteen years and that there were similar problems throughout the neighborhood. As the owner's two immediate neighbors had the same condition repaired in front of their homes, the Court stated that representatives of the Department of Public Works were presumably in the immediate vicinity of the open and obvious condition in front of the owner's house on at least two occasions. Therefore, the Court concluded

that the evidence presented by the neighbor was sufficient to raise a factual question of whether the municipality had constructive notice of the dangerous condition. The Court reversed the order granting summary judgment to the municipality and remanded the matter for trial.

LIMITED LIABILITY COMPANIES; "CORPORATE VEIL": Where the sole owner of a limited liability corporate subsidiary controls all the decisions of that subsidiary, the subsidiary will be viewed as the alter ego of the parent by that test alone. ***Cognex Corp. v. VCode Holdings, Inc., Slip Copy, 2006 WL 3043129 (D. Minn., Oct. 24, 2006),*** at * 1011

A Minnesota Federal District Court here addressed the issue of application of the alter ego theory to Illinois LLCs. VCode was a singlemember Illinois LLC with no employees of its own. Acacia Acquisitions ("Acquisitions") was a corporation and the single member. In turn, Acquisitions was wholly owned by Acacia Research Corporation ("Research"). The court held that VCode was the alter ego of Research, and the actions of VCode could be imputed to Research. The court permitted the plaintiff to proceed with its action for declaratory judgment against Research in connection with a patent dispute.

In its analysis, the court determined that Acquisitions and Research had nearly identical officers performing similar functions. The court also found that because no natural persons were part of VCode, all operational decisions on behalf of the LLC were in fact made by Acquisitions. The court noted that press releases and consolidated tax returns indicated that Research acted on behalf of VCode. The court further noted that Acquisitions was a holding corporation wholly owned by Research and had no assets other than its stakes in various subsidiaries, and that the officers of Acquisitions and Research were virtually identical.

Interestingly, the Minnesota District Court cites no other Illinois case on the application of alterego theory to Illinois LLCs. The court stated:

> "Like most states, Illinois law will impute the actions of a subsidiary to a parent where the subsidiary is an alter ego of the parent. The parent must exercise such control over the subsidiary that the two entities are indistinguishable. The actions of the subsidiary will then be imputed to the parent where necessary to prevent fraud or injustice [citation omitted]."

The parties to the case suggested that the court adopt a multiplefactor alterego test first (in connection with parent subsidiary liability) adopted by the Tenth Circuit in *Taylor v. Standard Gas & Elec. Co.*, 96 F.2d 693, 704 05 (10th Cir. 1938). But the court stated that

> "[t]his test is infrequently employed by Illinois courts, and there is little inclination that its use is currently favored." The court further noted that "[a]t the time that the test was developed, the law of business organizations had yet to recognize statutory limited liability companies," and "the underlying focus is whether the parent exercises such control that the parent and subsidiary are indistinguishable."

Comment 1: Acquisitions was a simple holding company, and conducted no business. Applying alter ego principles to that corporation seems appropriate. But Vcode did have a business. And it was incorporated to carry out that business. And the law of Illinois permitted the incorporation of single owner businesses. One would assume that, in a business with a single owner, that owner would have significant control over the affairs of the business. What is the meaning of the decision to permit incorporation of single owner businesses if not to permit business owners to enjoy the benefits of limited liability with respect to the affairs of that business, even though they in fact control the businesses decisions?

Although this case involves a corporate parent and a non-real estate business, the proliferation of single owner limited liability companies nationwide for purposes of ownership of real estate assets suggests that many real estate investors are relying upon LLC's to protect them from liability. Are they wrong? Are their attorneys, who take the money for forming these LLC's, wrong? Should the attorneys be advising greater separation in activity between LLC and owner? Exactly what sort of separation is appropriate?

Comment 2: Note that there were many other factors in this case that the court may have relied upon to conclude alter ego existed. For instance, apparently the subsidiary had no employees, and actions on behalf of the subsidiary were undertaken by employees and officers of the parent. But the court elected to look solely at the

question of control over decision making. It is this single-mindedness that provokes the Editor to report this case, as it strikes the editor that the same control over decision making exists with respect to many small LLC's.

Comment 3: This case follows hard on the heels of a recent Ohio case, *State ex rel Petro v. Mercomp, Inc*., 853 N.E. 2d 1193 (Ohio App 2006) *appeal denied* 855 N.E.2d 1258 (the DIRT DD for 8/24/06), an Ohio court held that the control by an individual who was the single owner/manager of an LLC rendered that individual personally liable for environmental fines levied against the LLC for decisions made in the course of the LLC's business.

MORTGAGES; DEFICIENCY; ANTI-DEFICIENCY LAWS; "SOLD OUT JUNIORS": What are the rights of a sold out junior to seek a deficiency following a Washington senior deed of trust private foreclosure, where Washington law states that there can be no deficiency judgment following a private foreclosure? ***Beal Bank v. Sarich, King Count Sup. Ct. No. 05-2-11440-1 SEA (9/27/06) appeal No. 5890270***

This case compels a determination of an issue left unresolved by the Washington Supreme Court when it decided *Washington Mutual Savings Bank. v. U.S.*, 793 P.2d 969 (Wash. 1990) *clarified upon denial of reconsideration* 800 P.2d 1190.

In *Washington Mutual,* a junior lienholder bought property at a private foreclosure sale conducted by a senior deed of trust lienholder. The IRS, a third lienholder, sought to redeem from the sale pursuant to its federal law redemption right. There was a disagreement about the price that the IRS should pay. Applicable law provided that the IRS would have to include claims of a junior lienholder purchasing at the foreclosure from which it redeems to the extent that such liens are satisfied by the sale. The law also provided that claims for which the junior lienholder has a deficiency claim would not be included as "claims satisfied by the sale."

The Washington Supreme Court ruled that the junior lienholder had no right to collect a deficiency amount unresolved after it purchased at the senior foreclosure sale because Washington law in general prohibits the collection of a deficiency following a private foreclosure under a deed of trust. The court's language in its original opinion was very sweeping and devoid of any complex reasoning:

> A[W]e hold here that [no deficiency judgment] may be obtained by a nonforeclosing junior lienor following a nonjudicial foreclosure sale. There is simply no statutory authority for allowing such a judgment following a nonjudicial, or deed of trust, foreclosure. Indeed, the tiel to RCW 61.24.100, part of the deeds of trust act, states flatly that '[d]eficiency decree precluded in foreclosure under this chapter'. We decline to create an exception to this statutory bar by judicial fiat."

Despite this broad statement, a concurring opinion attempted to reserve the issue of a junior seeking to sue on the note following the foreclosure of its lien. Later, in denying reconsideration, the whole court commented: "We do not herein address the matter of a junior deed of trust holder's continued right to sue the debtor on the promissory note because it is not before us."

Thus, Washington lawyers were left to puzzle out the difference between a "suit on the note" when one's lien has been sold out by a prior foreclosure sale, and a "deficiency judgment."

In the instant case, Beal Bank held a junior lien on a valuable condominium property. The lien secured a commercial debt. The senior lienholder foreclosed, and Beal, which had a pending foreclosure action to collect on its lien, amended its complaint to make that suit a claim on the note. Beal elected not to purchase the property at the foreclosure sale. In the brief of the borrower's counsel, there is lots of *ad hominem* arguing about the equities of the parties, but it appears that the court pretty much viewed its decision as based upon the law. It granted summary judgment for the borrower on the strength of the ruling in *Washington Mutual*, apparently viewing the suit on the note as effectively a deficiency claim, and thus barred by the holding of that case.

The case is now pending before the Washington Court of Appeals, and one of the parties suggested that the case might be interesting fodder for mortgage mavens on DIRT to chew upon.

Comment 1: To a certain extent, the fundamental problem here is the position of the Washington Supreme Court in *Washington Mutual* that it would not look behind the language of its foreclosure statute to identify the relevant policy considerations, interpreting the statute consistent with those considerations. Courts in California, Alaska, and Arizona, at least, in myriad decisions involving many aspects of anti-deficiency schemes, have reworked the statutory language to make the law into what the court believed the legislature meant, as opposed to what it might actually have said. In California, in particular, a number of lawyers and legal commentators have made a very fat living trying to explain and predict the court's efforts in this regard.

Perhaps mindful of that history, the Washington court held simply that the statute says no deficiency and that's what it means. In that case, the issue, due to the way the case came up, focused directly on whether an action termed an action for a "deficiency" might be available. The statute, it held, was clear on that point.

But the *Washington Mutual* case did nothing to explain its suggestion that there might be a difference between a pure "deficiency" judgment and an action on the note following the destruction of one's security at a prior lien foreclosure.

Comment 2: We should differentiate claims made by a junior who joins in the senior sale at a judicial foreclosure. Where the junior seeks a judgment in the senior's foreclosure, then clearly any unsatisfied balance remaining after application of foreclosure proceeds is a "deficiency." But in a senior deed of trust foreclosure the junior typically cannot join in the foreclosure. At best, it can seek to impose an equitable lien on the surplus proceeds, perhaps garnishing them in the hands of the foreclosing trustee. Beal Bank did not do that in this case.

Comment 3: Unlike California, Washington does not have a one form of action rule compelling a lender to foreclose rather than to sue on a note. Consequently, Beal Bank, in fact, could have sued on the note directly at any time prior to the senior's foreclosure, and even have obtained a judgment. As, in such instance, Beal Bank would have been waiving its right to foreclose its lien, it would be difficult to characterize such judgment as one for a "deficiency."

Why should we characterize Beal Bank's claim any differently where it elects to sue on the note following the non-judicial senior foreclosure?

Comment 3: The reason that we may be compelled to make such characterization is that the same argument could have been made about Washington Mutual's right to sue on the note in the precedent case. As a practical matter, there was no law that said that Washington Mutual was precluded from suing on its note despite the fact that it had purchased the property securing that note at a prior foreclosure that had wiped out Washington Mutual's lien. Was the Washington Supreme Court admitting that such a lawsuit would be distinct from a "deficiency?" It is difficult to read the *Washington Mutual* case as based so completely on semantics. But there is no reason in the statutes to differentiate the situation of a junior who buys at the senior's foreclosure and later pursues and action on the note and one who does not buy at the senior foreclosure and wishes to pursue such an action.

In short, the Washington courts should rework *Washington Mutual* and explain what difference exists, if any, between the collection rights of a junior who buys at a senior foreclosure sale and one who doesn't. In the editor's view, there is no difference and either part should be free to sue on the note, and the statute should not bar such suit. To the editor it is immaterial whether we should characterize such as suit as a "deficiency," since the real purpose of the Washington statute barring deficiencies following non judicial foreclosures is to limit the rights of the foreclosing senior.

MORTGAGES; FORECLOSURE; FAIR DEBT COLLECTION: Under the Fair Debt Collection Practices Act, a debt collector (which includes an attorney regularly engaged in debt collection activity), need only include, in its initial communication to a borrower, notice that it is attempting to collect a debt and that any information obtained would be used for that purpose; and once that notice has been given, it is not necessary to include the notice within subsequent communications. A foreclosure Complaint may be the "first communication". ***Barrows v. Chase Manhattan Mortgage Corporation, 2006 WL 3626883 (U.S. Dist. Ct. D. N.J. 2006) 12/06/06)***, discussed under the heading: "Fair Debt Collection; Foreclosure."

MORTGAGES; MORTGAGEE IN POSSESSION; COMMON FEES: A mortgagee in possession of a

condominium unit is personally liable for delinquent condominium common charges which accrue against the property's legal owner for services furnished during the mortgagee's possession and control of the premises. ***Woodview Condominium Association, Inc. v. Shanahan, 391 N.J. Super. 170, 917 A.2d 790 (App. Div. 2007)***

A mortgagee in possession of a condominium unit never paid monthly condominium fees while in possession and control of the premises. Consequently, the condominium association sued the mortgagee in possession for conversion and on a book account. The mortgagee defended the action, alleging that it was not personally liable for the accrued fees because it did not hold legal title to the units. The lower court ruled against the mortgagee, reasoning that the mortgagee could not avoid responsibility for all mandatory condominium fees, but still benefit from the rental value of the unit itself. The mortgagee appealed.

The Appellate Division affirmed, holding that along with the entitlement to profits and rent, mortgagees in possession assume the duties of a provident owner which requires management and preservation of the property. The Court then held that a mortgagee in possession may be liable for services rendered to it in connection with the property during its occupancy on the basis of an express or implied contract. The Court found the mortgagee entered into an implied contract in which it received the benefit of common services and so had to suffer the burden of their cost. Accordingly, the Court remanded to the lower court to answer the narrow question of when the mortgagee took possession of the unit so as to appropriately adjust the amount of the judgment based on that determination.

MORTGAGES; PREPAYMENT; PREPAYMENT PENALTIES; BANKRUPTCY: A prepayment premium secured by a mortgage on the debtor's homestead should be considered when determining the amount of "all other liens on the property" for purposes of Sec. 522(f)(2)(A)(ii) of the Bankruptcy Code. ***In re Barrett, 2007 WL 1544658 (Bkrtcy D. Me. May 29, 2007)***

This case decides what may be a case of first impression. The court termed it a "novel issue". The court concluded that the prepayment premium was a "cognizable component of the claim secured by an unavoidable mortgage", and since the judicial lien of another creditor, Precision, impaired the debtor's homestead exemption, it would be avoided

Sec. 522(f) of the Bankruptcy Code permits debtors – with the objective of providing a "fresh start" for the debtor – to avoid a judicial lien to the extent "it impairs an exemption to which the debtor would otherwise be entitled.") The debtor in this case had a homestead exemption. The value of CIT's "unavoidable lien" (i.e., the principal balance of the mortgage ($447,712) and the prepayment premium ($22,386), combined with the claimed homestead exemption ($70,000)), according to the court, "was greater than the stated value of the property ($540,000)." Therefore, the court totally avoided Precision's judicial lien ($12,595.74) because "it impaired the exemption to which the [debtor] would otherwise be entitled."

Reporter's Comment 1: But when all the figures (including the prepayment premium) are added up, the "impairment" of the debtor's exemption is exactly $98.04! This appears to be another results-oriented decision, with the court wanting to make as much money available as possible for distribution to unsecured creditors and preserve the debtor's homestead. (The court noted that "Without inclusion of the prepayment penalty in CIT's secured claim, Precision's judicial lien would not impair the [borrowers] homestead exemption."

Reporter's Comment 2: Note that here the first-mortgage lender, CIT, had not declared a default or accelerated its loan prior to the debtors' bankruptcy. Especially if the language in the prepayment provision did not provide that acceleration of the debt or any voluntary or involuntary payment of the debt would trigger the prepayment premium, it is at least arguable that the prepayment premium provision would not be an enforceable (as opposed to hypothetical and unmatured) obligation on the date of the debtor's bankruptcy filing. *See, e.g., In re Hidden Lake Ltd. Partnership*, 247 B.R. 722 (Bankr. S.D. Ohio 2000), where the court addressed the issue, raised by the debtor, of whether the prepayment charge constituted a claim for unmatured interest, which is barred by § 502(b)(2) of the Bankruptcy Code. The court ruled that because the claim for the prepayment premium arose as the result of acceleration of the indebtedness prior to the debtor's bankruptcy, the charge had matured at that time and therefore could not

constitute a claim for unmatured interest. However, the court noted that "[h]ad Aetna's note contained an acceleration right exercisable upon the filing of a bankruptcy petition and had there been no prepetition acceleration, the result might be different." Id. at 730. (emphasis added.)

In *In re Ridgewood Apartments of DeKalb County, Ltd.*, 174 B.R. 712 (Bankr. S.D. Ohio 1994), where the borrower filed a voluntary petition under Chapter 11 of the Bankruptcy Code. The lender, Fannie Mae, had accelerated the entire debt prior to the filing of the bankruptcy petition and filed a claim in the bankruptcy proceeding that included a prepayment premium in the amount of $263,275, as established by a formula attached as an Addendum to the promissory note. Fannie Mae contended that the prepayment premium had been validly triggered by the acceleration of the debt. The prepayment provision provided that the premium would be due whether the prepayment was voluntary or involuntary. But the court held that actual "prepayment" of the loan was initially required, regardless of whether the payment was "voluntary" or "involuntary", in order to invoke the penalty in the first place, and because the borrower had not in fact prepaid the note and did not contemplate prepayment under its bankruptcy plan under the original terms of the loan, no prepayment penalty was due and owing prior to or at the time of the bankruptcy filing. Therefore, the court ruled that the prepayment premium calculated by the lender was a "contingent liability" and not properly part of the lender's claim. The court also held that (after – rightfully – acknowledging that several bankruptcy decisions allow the lender to collect a prepayment premium when the provision specifically states, as in this case, that the premium is due upon acceleration of the debt) because the claim was for contingent interest which was not yet due and payable at the time of the borrower's bankruptcy filing, it would also be disallowed to the lender, an undersecured creditor, as unmatured interest under § 502(b)(2) of the Bankruptcy Code. The court stated that, because it had found the prepayment provision unenforceable under § 502(b)(2), it "need not . . . render a determination on the enforceability of the prepayment penalty based solely upon an acceleration by the lender." Id. at 721. *See also Continental Securities Corp. v. Shenandoah Nursing Home Partnership*, 188 B.R. 205, 213214 (Bankr. W.D. Va. 1995) ("to the extent § 502 would disallow a claim for unmatured interest, it is relevant here since that is essentially what [the lender] is seeking. Were the bankruptcy court to hold that that [the borrower] must pay [the lender] the full value of the Note through its maturity, it would essentially be allowing the payment of unmatured interest which is prohibited by § 502.").

Reporter's Comment 3: But the majority view is that a prepayment premium does not constitute unmatured interest under § 502. *See, e.g., In re Tri State Ethanol Co., LLC,* 354 B.R. 913, 918 ("the prepayment charge was fully due and owing on the date Debtor filed its petition. Thus, it cannot represent unmatured interest" [under § 502(b)(2)]); *In re Outdoor Sports Headquarters, Inc.,* 161 B.R. 414, 424 (Bankr. S.D. Ohio 1993) ("Prepayment amounts, although often computed as being interest that would have been received through the life of the loan, do not constitute unmatured interest because they fully mature pursuant to the provisions of the contract. . . . As a result of the parties' contractual agreements, reflected in the terms of the Notes and mortgage, the [lender] has a right to receive this payment if payment of the entire amount due pursuant to the Note is made prior to the full term of the contract. Therefore, the Prepayment Amount does not constitute unmatured interest and will not be disallowed pursuant to § 502(b)(2)"); *In re Skyler Ridge*, 80 B.R. 500, 508 (Bankr. C.D. Cal. 1987) ("[l]iquidated damages, including prepayment premiums, fully mature at the time of breach, and do not represent unmatured interest" under § 502(b)(2)); *Boyd v. Life Ins. Co. of the Southwest*, 546 S.W. 2d 132, 133 (Tex. Civ. App. 1977) (holding that "[a] prepayment charge on a promissory note is not compensation for the use of money. Rather, it is a charge to the borrower for the privilege of repaying the loan before maturity. . . ."); *C.C. Port, Ltd. v. DavisPenn Mortgage Co.*, 61 F.3d 288, 289 (5th Cir. 1995) ("Where the contract grants the borrower the right to prepay, a prepayment premium is not compensation for the use, forbearance, or detention of money, rather it is a charge for the option or privilege of prepayment"); *In re 360 Inns, Ltd.*, 76 B.R. 573, 576 (Bankr. N.D. Tex. 1987) ("the prepayment penalty was not unmatured interest as contemplated in § 502(b)(2), inasmuch as the prepayment penalty was activated and matured once the plan of reorganization proposed to pay [the lender's] debt"); *In re Hidden Lake Ltd. Partnership*, 247 B.R. 722, 730 (Bankr. S.D. Ohio 2000) (finding that because the claim for the prepayment premium arose as the result of acceleration of the debt prior to the debtor's bankruptcy, the charge had matured at that time and therefore could not constitute a claim for unmatured interest); *In re Lappin*

Electric Co., Inc., 245 B.R. 326, 329 30 (Bankr. E.D. Wis. 2000) ("this court is in agreement with a majority of courts that view a prepayment charge as liquidated damages, not as unmatured interest or an alternative means of paying under the contract [citations omitted]. In this case, the charge is independent of the amount owed at termination, thus negating any characterization as interest"); *In re TriState Ethanol Co. LLC*, 354 B.R. 918, 918 (Bankr. D. S. Dak. 2006) ("the prepayment charge was fully due and owing on the date Debtor filed its petition. Thus, it cannot represent unmatured interest").

Reporter's Comment 4: In any event, this case involves a very unusual fact situation of apparently first impression, with the prepayment issue being only tangential to the court's ruling. It also involves a residential loan, thereby invoking Sec. 522(f) of the Bankruptcy Code, which enables the debtor or trustee to avoid a judicial lien to the extent "it impairs an exemption to which the debtor would otherwise be entitled." Many states severely restrict or even prohibit prepayment premiums in connection with residential (but not commercial) loans. Federal associations may include prepayment penalty clauses in commercial loan documents and enforce such clauses according to their terms regardless of any state law to the contrary (including equitable principles) because C.F.R. § 545.2 and 545.34(c), as amended at 49 F.R. 43044, authorize a Federal association to include a prepayment penalty clause in any loan it makes and to enforce such a clause in accordance with its terms regardless of any state law including equitable principles in a foreclosure action which purports to prohibit the collection of a prepayment penalty under certain circumstances. The preemptive effect of these regulations applicable to Federal associations is subject only to the limitations with respect to loans secured by borrower occupied homes found or referred to in 12 C.F.R. 545.34(c) (governing disclosure and the imposition of a prepayment penalty after notice of an adjustment of an adjustablerate mortgage) and the final rule regarding prepayment penalties with respect to residential property set forth in 12 C.F.R. § 591.5(b). However, other federal legislation has limited or prohibited prepayment premiums or fees in connection with FHA loans (12 C.F.R. § 545.6 12(b); Veterans' Administration loans (24 C.F.R. § 207.253(a)); certain "high cost loans" (12 C.F.R. § 226.32), certain manufactured home loans (12 C.F.R. 590); and loans made by lenders subject to Federal Home Loan Bank Board regulations (38 C.F.R. § 36.4310).

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

MORTGAGES; PRIORITY: Timber deed of trust has priority over subsequent UCC filing. ***Feliciana Bank & Trust v. Manuel & Sessions, L.L.C., 943 So. 2d 736 (Miss. 2006).***

Feliciana Bank & Trust Company loaned money to Ducote and secured the loan by a deed of trust on land in Wilkinson County, Mississippi. Ducote subsequently contracted to sell the timber on the land to Manuel & Sessions, L.L.C. (there are some factual questions about whether Manuel & Sessions was the real purchaser, but those questions are not relevant to the real property issue.)

Manuel & Sessions cut and sold the trees and paid the proceeds from the sale to Ducote and others involved in the cutting. Ducote did not apply the proceeds from the sale to his loan.

The bank subsequently foreclosed on the land. The proceeds of the foreclosure sale were less than Ducote's indebtedness to the bank. The bank brought an action for waste against Manuel & Sessions.

Although there are numerous cases decided prior to the enactment of the UCC which followed the common law rule that the timber remains part of the realty until severed, there are no cases in Mississippi that address this issue after the enactment of the UCC.

Manuel & Sessions argued that, under the Uniform Commercial Code as in effect in Mississippi ("UCC") (all relevant provisions of the UCC are the uniform versions), the security provided by the bank's deed of trust was extinguished as to the timber when Ducote signed a contract to sell the timber. They claimed that the UCC changed the law and that once a contract for the sale of the timber existed, the only way for the bank to obtain security interest in the timber was to file a financing statement. The bank asserted that it had filed a financing statement, but the court characterized the bank's compliance with the UCC as "questionable". The trial court held that once the contract had been signed, the UCC cancelled the bank's interest in the timber under the deed of trust, and the only way for the bank to perfect a security interest in the timber to be cut was to file a financing statement. Since the bank's deed of trust apparently did not meet the requirements of a financing

statement covering timber to be cut, the trial court reasoned, the buyer took free of the bank's interest.

The definition of "goods" in Article 9 of the UCC includes "timber to be cut and removed under a conveyance or contract of sale." Subsection (2) of Section 2 107 of the UCC provides in relevant part, "A contract for the sale apart from the land of . . . timber to be cut is a contract for the sale of goods within this chapterYeven though it forms part of the realty at the time of contracting, . . ." Subsection (3) of Section 2 107 provides, "The provisions of this section are subject to any third party rights provided by the law relating to realty records, and the contract for sale may be executed and recorded as a document transferring an interest in land and shall then constitute notice to third parties of the buyer's rights under the contract for sale."

On appeal the Mississippi Court of Appeals reversed the trial court on this issue. Once a lender has filed its deed of trust on the land and timber, the execution of a contract to sell the timber does not cancel the lender's interest; rather, the purchaser of the timber takes subject to the lender's deed of trust. The UCC does not evince any intent to terminate the interest of an existing deed of trust in the timber. Section 9 2 107(3) of the UCC indicates that the intent was that the existing interest in the timber created by the deed of trust would continue and maintain its priority in the timber to be cut after the contact to sell was signed.

Reporter's Comment 1: The Reporter did some quick research under Section 2 107 of the UCC, and this case appears to be one of first impression on this issue. The reason for this may be that the result should be obvious; any other result would greatly diminish the value of timber lands as collateral. The intersection between the UCC and real property law in this context is sufficiently murky, however, that able defense counsel was able to convince an experienced trial judge to reach a different result in this case.

Reporter's Comment 2: IIn addition to filing a financing statement, a lender loaning money secured by timber lands can protect itself by making sure that its deed of trust also qualifies as a financing statement covering timber to be cut. The UCC expressly contemplates in Section 9 502 (c) that a deed of trust can serve as a financing statement covering timber to be cut, as well as as extracted collateral, and also serve as a fixture filing. It is important, however, to distinguish between a deed of trust serving as a financing statement and a fixture filing. When a deed of trust serves as fixture filing, the fixture filing does not lapse until the deed of trust is cancelled. UCC 9 515(g). A deed of trust that also is a financing statement covering timber to be cut or as extracted collateral is subject to the general five year lapse rule as to that type of collateral.

Reporter's Comment 3: In this case Manuel & Sessions did not file a copy of its contract. Would that have made a difference? Under the court's ruling, the result in this case should have been the same. If the purchaser had filed a copy of its contract, and then a judgment was filed against the owner/seller of the timber before the sale is finalized, would the filing of the contract permit the purchaser to take free of the judgment?

Reporter's Comment 4: The statement in Section 2 107(3) that the buyer can protect itself by filing the contract for sale in the land records raises a number of questions. Is the buyer protected if it files only a memorandum of the contract rather than the contract itself? The seller and buyer may want to keep the financial terms of a contract confidential. What if the buyer filed a financing statement in the land records giving notice of the sale would that be sufficient? Also, how does this statute work with other statutes that require that every instrument to be recorded in the land records must meet certain requirements? For example, Mississippi requires that every instrument to be recorded in the land records must identify the preparer of the instrument, show the indexing instructions so that the instrument can be properly indexed, and be acknowledged by a notary public. A typical contract for sale of timber would not meet these recording requirements. Is there any possibility that such a contract would be considered a "record" under Section 9 516 of the UCC, which limits the grounds on which a clerk can refuse to record a document?

Reporter's Comment 5: The *Feliciana* court stated, "Under the UCC, though, if a typical deed of trust is executed after a contract for the cutting of the timber has been executed but before the actual harvesting of the trees, the deed of trust will either not apply to the timber at all because the timber is now personalty, or else the deed of trust will be subordinate to a prior UCC filing." If the owner of the land and a buyer execute a contract for sale of timber, but do not file the contract (or otherwise

give notice of their contract) before a deed of trust is filed, shouldn't the beneficiary of the deed of trust have priority? Would it make a difference if an inspection of the property would have shown evidence that someone was about to cut the timber?

The Reporter for this case was Rod Clement of the Jackson, Mississippi Bar.

MUNICIPAL LAW; DEDICATION; ACCEPTANCE; PARKS: When lands are sold with reference to a map upon which appear a dedication of certain areas to the public as a park, but there is no immediate acceptance of such dedication, this establishes an offer of dedication that cannot be revoked except by consent of the municipality; therefore, when the affected property is sold, even in a tax sale, it is sold subject to the municipality's right to accept the dedication. ***Township of Middletown v. Simon, 387 N.J. Super. 65, 903 A.2d 418 (App. Div. 2006); July 31, 2006.***

Developers subdivided a tract of vacant land into fifty-seven lots for residential development. Fifty-six of the lots were numbered, and one lot, designated on the map as "Park", was unnumbered. The municipality approved the subdivision and developers recorded the approved subdivision map. Although the proposed subdivision was located on a lake, only twenty of the fifty-six numbered lots and the lot designated as a park afforded direct access to the lake.

Developer later appeared to try to develop a restricted subdivision and sold off a number of lots, but only a few of the deeds referred to the park parcel as subject to an easement of use.

For tax purposes, the park lot was initially appended to an adjoining lot and given only a nominal assessment. When the adjoining lot was sold, a question arose as to whether its boundaries corresponded with the tax records. To resolve this problem, the tax assessor gave the park lot a separate lot designation and assessment. Because the assessor was unable to identify the owner of this lot, the tax records indicated: "Owners Unknown". Thereafter, no taxes were paid for this lot.

Eventually, the municipality sold a tax sale certificate for the park lot to an investor, who subsequently paid delinquent taxes on the lot as well as the interest and costs of the tax sale. Later, the investor brought a tax foreclosure action seeking title to the park lot. Those opposing the foreclosure action filed an answer contending the municipality was an indispensable party to the tax foreclosure action because the subdivision map recorded by the couple had dedicated the lot as a park, and the municipality had a continuing right to accept the dedication. The lower court rejected this contention and held that the park had not been dedicated to public use.

The investor subsequently entered into a contract to sell the lot to a new developer who planned to construct a residence on it. When these plans became known, the owners of homes in the lake development voiced objections to the municipal governing body, claiming that the park lot was dedicated for park use and therefore could not be developed.

The municipality then filed this particular action against the investor and the developers, seeking a declaration that the park lot had been dedicated for use as a park. During the pendency of this action, the municipality's governing body adopted an ordinance accepting dedication of the park lot.

At trial, the lower court concluded that the municipality was in privity with the property owner who opposed the tax foreclosure action, and therefore, the municipality was barred under the doctrine of *res judicata* and collateral estoppel from relitigating the ruling in the foreclosure action that the park was not dedicated to public use. The lower court also indicated that even if the municipality had not been barred from relitigating the issue, it would have concluded that the park lot had not been dedicated to public use. Accordingly, the lower court dismissed the municipality's complaint. The municipality appealed.

On appeal, *Held: Reversed:* The municipality is entitled to prove a dedication to public use.

In addressing the argument that the municipality was barred by collateral estoppel from asserting that the park lot was dedicated to public use, the Appellate Division explained that to foreclose relitigation of an issue based on collateral estoppel, the party asserting the bar must show that: (1) the issue to be precluded is identical to the issue decided in the prior proceeding; (2) the issue was actually litigated in the prior proceeding; (3) the court in the prior proceeding issued a final judgment on the merits; (4) the determination of the issue was essential to

the prior judgment; and (5) the party against whom the doctrine is asserted was a party to, or in privity with, a party to the earlier proceeding.

The Court found that the issue of whether the couple dedicated the park lot for public use was actually litigated in the foreclosure action, and the identical issue was presented in this case. Furthermore, the tax foreclosure action resulted in a final judgment in the investor's favor. Consequently, the investor had established the first three prerequisites for collateral estoppel. However, the Court concluded that a finding of whether the couple dedicated the park lot was not essential to the judgment in the tax foreclosure action, and therefore, the fourth prerequisite for invocation of collateral estoppel to bar relitigation of this issue had not been established.

The Court then discussed the interest a municipality acquires when land is dedicated for public use and the interest a foreclosing party acquires when a final judgment is entered in a tax foreclosure action. When a private property owner dedicates land for public use, he or she makes an offer of a public easement and the municipality has a continuing right to accept the dedication at any time, unless it rejects the dedication by official municipal action. Until the municipality accepts the dedication, it acquires no interest in the land. When a party acquires title to property by a tax foreclosure action, that party only acquires the fee interest in the land that was subject to taxes. Consequently, if the former owner dedicated the property to a public use, a party that acquires title by a tax foreclosure action takes the property subject to the public use and the municipality's continuing right to accept the dedication. In light of this analysis, the Court concluded that the determination whether the couple dedicated the park lot for use as a park was not essential to the judgment in the tax foreclosure action.

The municipality had not accepted the alleged dedication until it adopted an ordinance for this purpose. Thus, even if the original developer made a valid dedication of the lot for use as a park, that developer and its successors in title continued to own the lot and remained subject to property taxes. Therefore, the Court held that the lower court's conclusions in the foreclosure action regarding the dedication of the park lot for public use were unnecessary *dicta* and for that reason, did not prevent the municipality from relitigating the issue in this case.

The Court explained that when lands are sold with reference to a map upon which lots and streets are delineated, and there is a dedication of certain of the property on the map to the public, such dedication continues and cannot be revoked except by consent of the municipality. The Court found that the couple's recording of the subdivision map and subsequent sale of residential lots with reference to that map constituted an irrevocable dedication of the lot for public use as a park. Thereafter, the public rights conferred by the dedication could only be destroyed by proper municipal action. The Court reasoned that the conveyances of remaining lots in the subdivision by reference to the filed map reinforced the conclusion that the couple made an irrevocable dedication of the park lot for public use as a park.

Further, despite the dedication of the lot for use as a park, it remained subject to taxes. When the taxes were not paid, the municipality had a right to issue a tax sale certificate, and the investor acquired valid title to the lot in the tax foreclosure action. But the title was subject to the dedication of the land for use as a park, just as it would have been if the original developer had retained title to the lot or sold it to a third party. Therefore, the municipality's issuance of a tax sale certificate for the lot and the tax foreclosure judgment vesting title to the lot in the purchaser were not inconsistent with the Court's conclusion that the lot is dedicated for use as a public park.

Lastly, the Court rejected the argument that the municipality's claim that the park lot was dedicated to public use, and its subsequent acceptance of that dedication, was unfair to the investor and the developers. The Court reasoned that the investor and the developers had record notice of the subdivision map that designated the lot for use as a park, and an inspection of the lot would have revealed that it was developed and maintained as a park providing access to the lake. It further found that the investor and the developers had to have been aware that they would be able to construct a house on the lot only if neither the municipality nor the owners of other lots in the lake development attempted to enforce the dedication; or if the investor and developers were able to persuade a court that the filed subdivision map had not resulted in a dedication of the lot for use as a park.

Editor's Comment: The New Jersey approach here is hardly the universal rule. At least with respect to streets and roads, many states have statutes that require

acceptance of a tendered dedication within a specified time period, or the dedication is void and the property reverts to wherever the court concludes it ought to revert.

Also see: Barry Simon Developments, Inc., v. Hale, Cas No. ED87452 (Mo. App. 10/24/06) (the DIRT DD for 10/27/06) A depiction of an easement of access on a PUD plan is sufficient to establish dedication of the easement under the "implied dedication from plat" doctrine, and such easement may benefit owners of land adjacent to the land depicted on the plan, who were "strangers to the grant" in that they were unrelated to the developers or purchasers of the property subject to the plan. *Nettleton Church of Christ v. Sandra Conwill*, 92 CA 01215 SCT (Miss. 2/20/97) (the DIRT DD for 6/4/97) Under statute providing that "all streets, roads, alleys and other public ways" set forth on an approved subdivision map will be deemed dedicated to the approving agency (city or county), the dedication will be deemed a dedication in fee, and not just an easement; and under an approved subdivision map showing a square in the center of the subdivision connected to the surrounding street system, the public square will be deemed dedicated according to the statute. *Kraus v. Gerrish TP.,* 517 N.W.2d 756 (Mich. App. 1994). (The DIRT DD for 8/18/95) Once a road easement by dedication has been tendered, the public agency may accept it whenever public necessity demands, unless the dedicator withdraws the offer of dedication by specific statements or by use of the land that is wholly inconsistent with the later creation of a public way.

Compare: Reagan v. Brissey, 832 N.E.2d 659 (Mass. App. Ct. 2005) (the DIRT DD for 2/13/06). An implied park dedication easement must be affirmatively proven. Although the intent to create an easement may be interpreted from circumstances existing at the time deed was created or conveyed, the simple statement on the plat map that lots are dedicated may not be enough, and was not enough here.; *Stafford v. Klosterman*, 998 P.2d 1118 (Idaho 2000) (the DIRT DD for 4/11/01) Roadway easement depicted on a subdivision plat but not accepted by the county highway district through endorsement of the plat are not public roads; consequently, there is no public right of use.

All prior DIRT DD's are on the DIRT website: www.umkc.edu/dirt

The Reporter for this item was Ira Meislik of the New Jersey Bar. The Editor has edited and revised the report substantially.

OPTIONS; LEASE/OPTION AGREEMENTS; EXERCISE: Where purchaser deposits substantial cash payment at outset of lease option period, and purchaser's "rent" thereafter corresponds closely to the varying payments on seller's underlying mortgage, purchaser may be viewed as having already exercised option, even though he dies nine years later without having formally exercised the option. ***Lee v. Bass, 2007 Westlaw 505386 (2/20/07) (opinion not yet finally approved for publication)***, discussed under the heading: "Vendor/purchaser; Lease Option; Exercise."

OPTIONS; "RELATION BACK": Tenant's option to purchase "marketable fee simple title" entitles tenant to acquire property free of below market leases entered into by landlord prior to tenant's exercise of the option. ***Van Carr Enter. v. Hamco, Inc.,2006 WL 649985 (Ark. 3/15/06),*** discussed under the heading: "Landlord/ Tenant; Options to Purchase."

SERVITUDES; RESTRICTIVE COVENANTS; MODIFICATION; CHANGED CIRCUMSTANCES: Maryland reaffirms traditional covenants doctrine – changed circumstances argument based upon neighborhood circumstances must show that original purposes can no longer be realized due to changed circumstances over a reasonable period of time. ***City of Bowie v. MIE Properties, Inc. 2007 Westlaw 1296247 (Md. 5/4/07)***

What makes this case interesting is not what the court did, which was to pretty much stick to established doctrine, with a few twists, but rather what it didn't do. Unlike the lower appeals court, the Maryland Court of Appeals elected to adhere to the clearly expressed intent of the parties in a restrictive covenant, giving the covenant every opportunity to prove its worth over time.

The case is also valuable because it deals with a University-related research park deal. There are lots of these around the country (in fact, around the world), and clearly not all of them are going to succeed – at least not in the originally conceived time frame. What does the law do when the project stalls? Will the "changed circumstances" doctrine void the use covenants requiring use as a technical center?

Here, the City of Bowie, which has no independent zoning authority (that belongs to the County in the Maryland system), in 1986 assisted in the development of a 466 acre parcel near the University of Maryland as the "Maryland Science and Technology Center." The City, pursuant to agreement, annexed the parcel, so that it would receive a variety of City services. In exchange the developers – at that time a partnership between the University of Maryland and a private development company – agreed to a set of use restrictions that required that only uses consistent with a high tech research and technology park would occur there. In fact, the covenant was quite specific – identifying fourteen specific activities that could occur on the land.

Unfortunately, the idea did not really work out, and the University of Maryland, apparently as permitted by the development agreement, withdrew from project. Later the developer declared bankruptcy. Ultimately the property passed through several hands into those of MIE, Inc.

MIE leased space to a dance studio. Apparently as a test of the continued validity of the covenants, City brought suit to enforce the covenant and MIE counterclaimed for a ruling that the covenant was no longer valid. The trial court upheld the covenant. The intermediate court of appeals reversed and remanded, stating that the lower court had used the wrong standard.

On appeal, the Maryland Court of Appeals reversed the intermediate appeals court, noting that the central issue in the case was the method of determining whether changed circumstances affected the validity of the covenant:. Here is how it characterized the disagreement and resolved it:

> "In determining whether the Covenants remain valid and enforceable in relation to their purpose, the Court of Special Appeals placed the burden on the City to prove 'that there is a reasonable possibility that the Maryland Science and Technology Center will be developed on the property'. This was incorrect. The burden to prove the validity of a restrictive covenant devolves upon the claimed beneficiary of the restriction only 'where [it is] not specifically expressed in a deed, to show by clear and satisfactory proof that the common grantor intended that [it] should affect the land retained as a part of a uniform general scheme of development.' In other words, a covenantee bears the burden of proving validity only when there is doubt as to whether a covenant actually encumbers a particular tract of land. That is not the case here.
>
> The proper legal standard for this inquiry is to examine whether, after the passage of a reasonable period of time, the continuing validity of the covenant cannot further the purpose for which it was formed in light of changed relevant circumstances."

Specifically, the high court rejected the notion that a "reasonable probability" standard applied, since, in its view, such a test would necessarily take into account the willingness of the current owner to seek to develop the property as intended by the covenants. If the developer did not wish to do so, then of course, there was a low probability that the project would be developed. This permits the covenantor to control its own destiny and flout the original contract intent.

Importantly, the high court further stated that the amount of time over which the change of circumstances is to be evaluated is critical. If the covenant states its own time limitation, this will be honored. If not, then the court will interpret a "reasonable time", taking the amount of time into account in judging whether the continued vitality of the original project truly is beyond salvage. It noted that typical tests of "changed circumstances" occur after 50 or 60 years, while in this case only 19 years had run since the covenants had been created. This relatively short term imposed a much greater burden on the developer to demonstrate that there was no likelihood that, over further time, the project would become feasible. Here, sifting through the testimony of the warring experts, the Court concluded that there was ample evidence that, over further time, a developer committed to making the project work could do so.

Comment: There is lots more in the case about the basic covenant interpretation doctrines of Maryland that any Maryland lawyer ought to study. And, of course, the facts and discussion ought to be studied by any lawyer interesting in challenging or defending research park covenants in circumstances like this.

SERVITUDES; RESTRICTIVE COVENANTS; "UNIFORM SCHEME" AMENDMENTS: After a developer establishes a uniform scheme for all lots in the

subdivision, and provides a method for amending such scheme, the developer cannot later unilaterally impose more stringent restrictions on some of the lots as the developer sells them, as this would represent a change in the scheme that must comply with the amending provisions. ***Multari v. Gress, 155 P. 3d 1081 (Ariz. App. 2007)***

In 1973, Developer of a subdivision sold a lot to Moltari and apparently recorded a Declaration, referred to in the deed, that included a set of restrictions. The Declaration stated that the restrictions applied to "each and every lot in the subdivision". These restrictions prohibited structures other than "residences and certain accessory buildings". The court here read this provision as implicitly permitting accessory buildings of any size. After an initial term of 30 years, the covenants automatically renewed for successive ten year periods unless an instrument signed by at least two third of the then owners of the lots has been recorded, agreeing to change said covenants in whole or in part.

The Developer continued selling lots in the subdivision, but at some early point began including a separate set of covenants in addition to the first. In 1976, Developer sold a lot in the subdivision to Gress' predecessor, and, simultaneous with the recording of that deed recorded a second and supplementary set of deed restrictions. One assumes the deed referred to these restrictions. The court states that the restrictions "benefited" both Gress' lot and Moltari's lots. Developer apparently recorded express covenants similar to both sets of restrictions on 32 of the 54 lots in the subdivision sold after the 1973 transfer to Multari.

The second set of restrictions identifies certain lots, include Multari's, that have a right to enforce their terms, and, among many other things, apparently, restricted the size and height of accessory buildings. Gress' wished to maintain an accessory building larger than that permitted by the 1976 restrictions and Multari's wished to prevent this.

The dispute here relates to the Molinari's and the Gress', so we don't know what the impact of the 1976 restrictions might have been on the 22 lots that were not bound by them expressly, nor is there any argument that failure to bind these other lots constituted a "change of circumstances" that might have created an enforcement problem for the remaining lots. It is hard to tell, but it appears that all owners bought with record knowledge of the 1973 restrictions.

The problem here has to do with the interpretation of the covenant as it applies in favor Multari's lot, a specific named beneficiary of the 1976 covenants.
The court held that Multari could not enforce the 1976 covenants, even though the intent of the parties was to confer enforcement rights on Multari's lot, because the imposition of additional covenants to lots already subject to the 1973 covenants altered the uniform scheme. The court ruled that *any* change in the uniform scheme required the consent of 2/3 of the owners of the lots.

The basis for the court's ruling is extremely sketchy, but appears to be that the basis for enforcement of subdivision covenants imposed by the developer is to facilitate a uniform scheme of development beneficial to all of the lots. Changes in the scheme after the original creation of it necessarily will alter the impact of the scheme on the various bound and benefited lots, and consequently it is inappropriate to permit the developer "willy-nilly" to later create new restrictions inconsistent with the original scheme. Quoting from a prior Arizona case, the court stated: "To permit individual lots within an area to be relieved of the burden of restrictive covenants, in the absence of a clear expression in the instrument so providing, would destroy the right to rely on restrictive covenants which has traditionally been upheld by our law of real property."

The court acknowledged that the concern was perhaps less acute, where, as here, additional restrictions are added, rather than releases given, but the problem with interference with a uniform scheme remains. The court stressed that here the original uniform scheme provided for a method of "changing" the restrictions – an instrument executed by two thirds of the lot owners. To change the restrictions in any way without such an instrument without complying with the amendment process was inconsistent with the original scheme.

The court attempted to differentiate the situation that might arise if subsequent owners got together to add new restrictions among themselves. This was proper, since it was not a change in the original scheme worked out by the developer. The court said that its injunction against changes without a formal amendment process applied only to the developer's attempts to institute changes.

Comment 1: The editor thinks he gets the idea, but must confess that the differentiation between subsequent changes instituted by other lot owners and those imposed by the developer on subsequent purchasers is a bit obscure. It may be that the facts aren't as fully developed concerning the 1976 covenants and their intended breadth. But let us assume, for instance, that midway through the sale process the developer identifies a market tool in the form of some kind of additional restriction that would be appropriate for some, but not all, the lots in the subdivision, and therefore begins imposing that new scheme within the identified area. So long as the new scheme does not restrict the ability of the other lot owners to enjoy the right to enforce the restrictions of the original scheme, why shouldn't this be possible?

If the homeowners are indeed subject to the same impact if carried out by individual groups of owners after the original scheme is established, what harm is there in leaving them exposed to the developer being able to carry out such a change?

Comment 2: It does seem anomalous, however, for the developer to permit non-burdened parcels, such as Mulnari's parcel, to enforce the special restrictions that arose later. That may be a critical fact in this case, but the court makes nothing of it.

STATE AND LOCAL TAXATION; PROPERTY TAX; TAX FORECLOSURE; CONSTITUTIONAL LAW: Michigan Supreme Court invalidates statute that would have permitted tax foreclosure authority to transfer irrevocable title to property in tax foreclosure even where authority had not provided notice to prior owner in accordance with statute or with Due Process. ***Wayne County Treasurer v. Perfecting Church, 2007 Westlaw 1518607 (5/23/07)***, discussed under the heading: "Constitutional Law; Due Process; Notice; Tax Foreclosure."

STATE AND LOCAL TAXATION; PROPERTY TAX; TAX FORECLOSURE; DEDICATED LANDS: When lands are sold with reference to a map upon which appear a dedication of certain areas to the public as a park, but there is no immediate acceptance of such dedication, this establishes an offer of dedication that cannot be revoked except by consent of the municipality; therefore, when the affected property is sold, even in a tax sale, it is sold subject to the municipality's right to accept the dedication. ***Township of Middletown v. Simon, 387 N.J. Super. 65, 903 A.2d 418 (App. Div. 2006); July 31, 2006.***, discussed under the heading: "Municipal Law; Dedication; Acceptance; Parks."

TITLE; ESTOPPEL BY DEED: If a grantor conveys land by warranty deed, but does not at the time of transfer have good title, the common law doctrine of estoppel by deed provides that title that is subsequently acquired by the grantor automatically inures to the benefit of his or her grantee, and the grantor and any later claiming under grantor are estopped from contesting that title. ***Rendleman v. Heinley, 140 N.M. 912, 149 P.3d 1009 (2006).***

Two chains of title leading from Guadalupe T. Lujan created an issue of whether Heinley's easement on the disputed property was valid or whether Rendleman owned the disputed property

The second chain of title indicated that in 1967 Domitilia Montoya conveyed the disputed property to Guadalupe T. Lujan. Then Guadalupe T. Lujan conveyed the disputed property to her daughter Margaret T. Lujan. This chain of title led to title in Rendleman.

The district court applied the after acquired title doctrine in favor of Fassler and held that Fassler owned the disputed property at the time she granted the easement to Heinley. The New Mexico Court of Appeals affirmed the district court's opinion and concluded that Heinley's easement was valid and did not constitute a trespass.

In reaching its conclusion that the district court properly applied the after acquired title doctrine, the Court of Appeals noted that "[c]ases from other jurisdictions show that, since early on, the after-acquired title doctrine was applied to vest title in the first grantee and those holding under him [or her] where there were two chains of title from one initial grantor."

Rendleman's lawyer made a spirited argument that the court should instead decide the case based on the strength of the two titles. He argued that since Rendleman's title came straight from the U.S. Government patent, it was the strongest. The court pointed out that, under the after-acquired title doctrine, Rendleman's title lacked strength, noting that when good title was eventually granted to Ms. Lujan, it immediately vested by operation of law in the first grantee, who was Mr. Heinley's predecessor in title, not in Mr. Rendleman's predecessor in title. Further, after

making the original conveyance to Mr. Heinley's predecessor in title, Guadalupe Lujan had nothing more to convey to Mr. Rendleman's predecessor in title.

Comment 1: Note that this "estoppel" is an equitable concept and depends upon the subsequent grantee having actual or constructive knowledge of the first deed by the common grantor. The court doesn't discuss the notice issue here, but it frequently is a big deal in these kinds of cases. The question is whether the prior deed, which typically was executed and recorded before the grantor passed into title to the property, is in "chain of title" for subsequent title searchers, so as to impart constructive notice to them. Some jurisdictions conclude that any recorded deed from a grantor in the chain of title provides constructive notice, even if made and recorded before the grantor ever got title. These jurisdictions we law professors call "long up" jurisdictions, and we criticize them as based upon a hypothetical title search that is wholly unreasonable. A title searcher would have to run back every title in the chain back, back, back. Here he would even have to run back before the patent from the government was issued. But there you are.

If the jurisdiction maintained a tract index, this issue might be moot, as a tract index might pick up all deeds recorded against this property, whenever recorded. (Note there was a side dispute about the validity of the description, which made this issue a bit more dicey.) Further, if there was a title insurance company involved in the second transfer, and it maintained a tract index, it might have picked up the competing title.

Obviously no one viewed the recording acts as making a difference in this case, so the second taker must have indisputably had constructive or actual notice of the prior deed. Or perhaps it had actual notice of the easement from evidence of it on the land, which put it on inquiry to discover the prior deed.

Comment 2: The editor once learned (can't say from where) that "estoppel by deed" is the term used to describe the common law version of the rule in question, involved here, and to use "after acquired title" to describe the statutory version that exists in many states. The court here uses the latter term to describe the common law version. Well, what's in a name?

Comment 3: In the statutory version in Missouri, there is no statement that the first deed must be a warranty deed – only that the grantor represents ownership. The editor has felt that getting a statement, made clearly without warranty, that the grantor believes himself to be the owner and so represents, might estop the grantor and his successors even in a quitclaim deed, and he bargains for it when he can.

TITLE INSURANCE; "INSURED"; TRANS-FER TO COMMON CONTROLLED ENTITY: New Jersey court rules that policy not terminated on transfer of property from insured general partnership to LLP, despite the policy's terms, because the partners reasonably expected policy coverage to continue. Shotmeyer v. New Jersey Realty Title Ins. Co., 2007 WL 283661 (N.J.Super.A.D.) (unpublished).

In 1981, New Jersey Realty Title Insurance issued a policy to Henry and Charles Shotmeyer, doing business as Beaver Run Farms, a general partnership, for two parcels in New Jersey. The policy contained standard language limiting the concept of "insured" so as to limit the benefits of coverage to purchasers from the insured. The conditions and stipulations section of the policy defines "insured" as follows:

"The insured named in Schedule A and, subject to any rights or defenses the Company may have had against the named insured, those who succeed to the interest of such insured by operation of law as distinguished from purchase including, but not limited to, heirs, distributees, devisees, survivors, personal representatives, next of kin or corporate or fiduciary successors."

Eleven years later, in 1992, Henry and Charles, ostensibly for estate planning reasons, formed a limited partnership, Beaver Run Farms, L.P., in which they were the limited partners and a corporation they owned was the general. They conveyed the property to the limited partnership for nominal consideration.

In 2002, Charles Shotmeyer learned that a neighbor claimed title to twelve acres of the property. He made a claim under the policy. Shotmeyer sued New Jersey Title after discussions about payment of diminution damages broke down.

The trial court held that the policy terminated on the transfer to the limited partnership, and that the insurer did not waive the coverage defense by conducting the settlement discussions. The appeals court reversed the

first holding, but affirmed that an insurer does not waive a coverage defense by discussing settlement with the insured.

The appeals court led off with the common statement that title insurance policies are to be "liberally construed in favor of the insured and strictly construed against the insurer", citing *Sandler v. N.J. Realty Title Ins. Co.*, 36 N.J. 471, 478-79 (1962). It noted that "[t]his, of course, does not mean that a court will rewrite a policy for the benefit of the insured." It then proceeded to do just that, by holding that the Shotmeyer brothers never transferred their "beneficial interests" in the land:

> "It is generally held that when title is passed by 'operation of law', the change is automatic or involuntary. ... However, a transfer by 'operation of law' is not necessarily automatic and is not so limited. For example, the identical definition of 'insured' that is involved in this case has been held to include a voluntary transfer of assets upon corporate dissolution. See Historic Smithville Dev. Co. v. Chelsea Title and Guar. Co., 184 N.J.Super. 282, 289 (Ch. Div.), aff'd, 190 N.J.Super. 567 (App.Div.1983). However, the focus on whether or not the transfer was by operation of law is misdirected. What is significant in this case is that there was never a transfer of the Shotmeyer brothers' beneficial interests in the lands the title insurance policy was procured to protect."

The court said that what mattered was the Shotmeyers' reasonable expectation of coverage:

> "The Shotmeyer brothers purchased the property and took title in the name of their general partnership, Beaver Run Farms. That general partnership then transferred the property to Beaver Run Farms, L.P., a newly created limited partnership of which they retained full ownership and control. The Shotmeyer brothers were the only individuals involved in each of those entities and the respective partnerships were merely vehicles for their ownership of the property.
>
> We recognize that ordinarily, '[p]roperty acquired by a partnership is property of the partnership and not of the partners individually." N.J.S.A. 42:1A-11. However, the title policy identified the individual partners and the partnership as insureds thereunder. Under such circumstances, Beaver Run Farms, L.P., though it is a distinct legal entity, is not a stranger to the title insurance policy. It is also comprised of Charles and Henry and a corporation in which they are the sole shareholders. In short, the general partnership and the limited partnership are no more than alter egos of Henry and Charles Shotmeyer. These partnerships may be compared to corporations, in that where two corporations are alter egos of one another, corporate form should be disregarded in the interests of justice. . . . It is critical that although the brothers changed the form of their ownership, they never relinquished control and never diluted their personal interests in the property that is the principal, if not the sole, asset of the artificial entities they formed to hold title.'
>
> The trial court deemed it significant that the general partnership, Beaver Run Farms, continued to operate after it transferred the property to the limited partnership. However, such continuing existence of the general partnership, does not necessarily militate against the finding urged by plaintiffs, that the title insurance policy issued for their benefit remains in effect. Where there was no change of substance, there was no reason for Charles and Henry to expect that the title insurance company would not recognize their continued ownership of the property. The suggestion in the Shotmeyers' appellate brief, that title can be reconveyed, if necessary, from the limited partnership to the general partnership, only serves to underscore the absurdity that results when form is exalted over substance.
>
> Equity always attempts to get at the substance of things, and to ascertain, uphold, and enforce rights and duties which spring from the 'real' relations of parties. It will never suffer the mere appearance and external form to conceal the true purposes, objects, and consequences of a transaction. [Historic Smithville Dev. Co., supra, 184 N.J.Super. at 293.]
>
> . . . Significantly, Charles and Henry did nothing to adversely affect the title to the property. The

> defect that threatened or occasioned the loss that led to this civil action existed at the time defendant issued the title policy for the Shotmeyers' protection. The Shotmeyer brothers did nothing to increase either the risk or the burden of the insurer. Charles and Henry's heirs are still the beneficial owners of the property. They reasonably expected the title insurance policy would protect them from defects that existed in the title of the land described in the June 18, 1981 deed from Mabel A. Day from the time of their acquisition and they are entitled to such protection."

The court held, however, that the insurer did not waive the right to contest coverage by offering to settle the dispute, particularly since the insured rejected the offer:

> " . . . [W]e . . . deem it prudent to address plaintiffs' argument that defendant waived any right it may have had to disclaim liability under the policy when it offered to settle the claim. We roundly reject that argument. Defendant acknowledged that the claim . . . 'may well present a compensable event. . . .' That acknowledgement was not a cognizable basis for liability. At most, it was an offer to settle the dispute, which plaintiffs rejected. . . . Thus, the motion judge appropriately concluded that defendant's acknowledgement, in the context of an attempt to settle a claim, did not rise to the level of waiver."

This ruling may prove useful to title insurers in other situations, since title insurers are often included to offer settlements or to take limited action to clear title even when they are not convinced there is policy coverage.

Reporter's Comment: New Jersey Realty Title appears to have made all of the applicable arguments, and the court simply resorted to the reasonable expectations doctrine to avoid them. The court's alter ego analysis is directly contrary to the more careful interpretation of the policy's terms found in *Gebhardt Family Investment, L.L.C. v. Nations Title Ins. Co. of New York, Inc.*, 132 Md.App. 457, 752A.2d 1222 (Md.App. 2000) (transfer to limited liability company terminated policy), *Gray v. First American Title Ins. Co.*, 2003 WL 220606 (Cal.App. 2 Dist.) (unpublished) (reh.den. 3/4/2003) (transfer to partnership terminated policy); *Point of Rocks Ranch, L.L.C. v. Sun Valley Title Ins. Co.*, 143 Idaho 411, 146 P.3d 677 (Idaho 2006) (transfer to limited liability company); and especially *Butera v. Attorneys Title Guar. Fund, Inc.*, 321 Ill.App.3d 601, 704 N.E.2d 949, 254 Ill. Dec. 537 (Ill.App. 1 Dist. 2001). The only other case that adopted an insurable-interest test was the loopy decision of *Heyden v. Safeco Title Ins. Co.*, 175 Wis.2d 508, 498 N.W.2d 905 (Dist. 1 1993).

Editor's Comment 1: "Loopy" or not – what's the matter with interpreting the title insurance company's own language in a way that comports with the reasonable expectations of the parties, so long as those expectations are not directly contradicted by the clear policy language.

Compare, also: Point of Rocks Ranch, LLC v. Sun Valley Title Ins. Co., 146 P.3d 677 (Idaho 2006, where the court held unequivocally that a transfer by deed to a wholly owned LLC is not a transfer "by operation of law".

Editor's Comment 2: The editor still fails to grasp the reasoning of title insurers in refusing to include wholly owned business entities of the insured under the coverage granted under the policy. If the policy extends to heirs and successors by operation of law, why not these entities?

The editor is reminded of a similar line of reasoning in *First American Title Insurance Co. v. Dahlmann,* 2006 Wi. 65, 2006 Wisc. LEXIS 358 (6/7/06), the DIRT DD for 8/23/06, where the court help that overlap of improvements on insured property onto neighboring property are insured under a policy in which the insurer has waived the title exception. Although there was some argument that the express language of the policy did not insure this problem, the court held that the insurer's waiver of the standard survey exception created the reasonable expectation of coverage.

Editor's Comment 3: Maybe the title industry is now coming round. The following is an excerpt from a posting by DIRT's title insurance authority Jack Murray – part of an extended discussion involving many postings that occurred in 2006:

> "Note that under the new 2006 ALTA policies the definition of 'Insured' contained in Condition 1(d) in the 2006 Owner's Policy and Condition 1(e) in the 2006 Loan Policy has been expanded and is a significant improvement over the 1970 and 1992 ALTA Policies. A policy of

> title insurance protects, for the most part, only the named Insured in the policy. Under the 1970 and 1992 Policies, with little exception, those who succeed to the interest of the property by operation of law, as opposed to voluntary conveyance, also fall within the definition of 'Insured'. However, determining what is a voluntary transfer, as opposed to a transfer by operation of law, has resulted in substantial confusion and uncertainty. The new definition for 'Insured' in the 2006 Owner's and Loan Policies more clearly defines the term 'Insured' and recognizes as an Insured, among other entities or persons not addressed in the 1970 and 1992 Policies, certain 'voluntary' conveyances by the named Insured that are made without receipt of valuable consideration, including, in the Owner's Policy, where the grantee is the trustee or beneficiary of a trust established by the named Insured for estateplanning purposes. (My thanks to Dena Cruz for supplying the foregoing summary.)"

The Reporter for this item was J. Bushnell Neilson, writing in the excellent Title Insurance Law Newsletter, March 2007. As usual, the editor has edited the report.

UCC; ARTICLE NINE; TIMBER; PRIORITY: Timber deed of trust has priority over subsequent UCC filing. ***Feliciana Bank & Trust v. Manuel & Sessions, L.L.C., 943 So. 2d 736 (Miss. 2006),*** discussed under the heading: "Mortgages; Priority."

USURY; IMPACT OF USURY ON CONTRACT; SPECIFIC PERFORMANCE: Court did not err in awarding specific performance of the remaining provisions of a lease containing an option to purchase the property at a usurious interest rate, and tenant did not waive the issue of usury by seeking specific performance. ***Van Carr Enter. v. Hamco, Inc.,2006 WL 649985 (Ark. 3/15/06)***

This case is discussed further under the heading: "Specific Performance; Usurious Interest Rate."

VENDOR/PURCHASER; CONDITIONS; MORTGAGE CONTINGENCY: Where a mortgage contingency states that it is deemed satisfied unless invoked before a date certain, but there is no "time of essence" clause in the contract, the seller has a duty to be reasonable in considering whether to grant an extension of that date. ***Jaramillo v. Case, 100 Conn. App. 815 (2007)***

Buyer offered to purchase property contingent upon his "obtaining of a first mortgage from an accredited mortgage company" in the amount of $1.556 million. The offer did not specify a date by which the buyer was to obtain the mortgage, as the offeror anticipated that a more formal contract would be executed later if the offer was accepted. Buyer represented that he was "prequalified". The sellers accepted the offer and a formal contract of sale ultimately was executed. As attorneys were involved, however, the execution of the contract occurred some time after the actual acceptance of the offer.

In accepting this offer, sellers turned down another lower offer for full cash (contingent on inspection). Those offerors apparently remained "back ups" to this contract, even to the time that litigation ensued on it.

During the course of negotiations over an issue concerning the roof, seller informed the buyer that he would be making irrevocable arrangements concerning the caretaker of the property (it was a $1.8 million vacation place. . . sigh. . .) and that the sellers were counting on the buyer's commitment to proceed. The contract was executed shortly thereafter, calling for satisfaction of the financing contingency within about two weeks – on November 5. The contingency stated that if the buyer did not invoke the contingency by 5 PM on the date set, it was deemed satisfied. If the buyer did invoke it, the contract was cancelled and the buyer's earnest money would be refunded. Aside from these specified dates, and a specified closing date two months later, there was no general "time of essence" clause.

Buyer's appraiser looked at the property on November 1, but needed more information. He contacted seller's attorney, who was on vacation, and, instead of seeking an alternative source of the information he needed, just waited for a return call. On November 4, buyers asked for an extension of the mortgage contingency until November 12. Sellers countered that they would extend to November 9, and further if there were satisfactory explanations of the need for further delay. Seller had a discussion with Buyer's attorney in which he discovered the fact that the lender was reviewing tax returns and other issues, but the discussion became "heated" and was not concluded with full understanding or resolution.

On November 9, Buyer asked for a further extension, and indicated that the reason was that the mortgagee was reviewing the Buyer's income tax filings. By this time it was probably two months since Buyer had indicated in his original offer that he was "prequalified". The extension request indicated that if Seller did not agree to the extension, Buyer would have no choice but to ask for a refund of the earnest money. Sellers refused to grant the extension. Buyer's lawyer responded that he deemed the refusal "unreasonable" because the delay was due to the problem in getting appraisal information. Sellers then contracted to sell the property to the back up buyers for a price just a bit lower than Buyer's offer (perhaps some was eaten by brokers) and without a mortgage contingency.

Two days later, within the time period of the requested (but denied) extension, Buyer's lender approved the mortgage. The commitment was slightly lower than the amount specified in the contract and had further conditions – such as a certification from Buyer's accountant that the payment obligations would have no adverse impact on his business and, perhaps even more significant, and contract of sale on Buyer's current residence, which was not yet on the market. Sellers refused to proceed with Buyer. (The parties later disputed whether this was a "real" condition, but in any event it was after the Sellers' contested decision to deny further extensions. On November 30, Buyer waived the contingency and demonstrated the financial ability to close. But by then Sellers were committed to sell to the "back up" buyers for cash.

Buyer brought suit for specific performance, with a *lis pendens*. Sellers proceeded to close with the "back up" buyers subject to a litigation contingency.

The trial court found for sellers and the Buyer, apparently flush with litigation money, at least – appealed. On appeal, Buyer argued that, as there was no "time of essence" agreement, the seller had a duty to be reasonable in agreeing to extensions. Buyer contended that the trial court had applied a subjective, rather than an objective, standard in determining that Sellers had been reasonable, as the trial court had stated that the Buyers had acted out of perceived necessity rather than malevolence. Sellers had already purchased a replacement vacation home and were uncomfortable carrying two mortgages. Further, as they had dismissed their caretaker, they were concerned about closing before the onset of winter.

The appeals court affirmed, on the basis that the seller had been reasonable. Seller had communicated to the Seller at least some of the concerns leading it to desire an early closing. Buyer had been vague about why the extensions were needed, and, the court held, any seller would be suspicious if a seller had indicated eight weeks before that it was "prequalified" and now the lender was demanding to inspect tax returns.

Editor's Comment 1: Certainly the right result. And the right focus on the objective reasonableness of the Seller's decision as of the time of the decision. But the Connecticut lawyer who sent this in is concerned about the court's statement that the seller does not have an *absolute* right to refuse to extend a mortgage contingency written in this way. Here is that analysis:

Reporter's Comment: [This decision is] certainly alarming from a seller's perspective, as it focuses not on whether the buyer got his mortgage within a reasonable time of the specified date (no time of the essence clause in the contract), but rather on the reasonableness of the seller's rejection of a request for an extension. It is news to me that the seller is under some duty to entertain any request for an extension in the time within which a buyer might get his mortgage. Notice that in this case the buyer was careful not to waive the contingency in the face of the sellers' rejection of the extension request; rather, the buyer sought to preserve his right to terminate the contract.

I thought a seller could decline such a request for any reason or for no reason. By turning down the request, the seller of course runs the risk that the buyer gets the mortgage within a reasonable time after the specified date and demands that the seller perform; a threat to do so might chill efforts to line up another buyer. Apart from this risk especially difficult to gauge here because Connecticut cases offer no practical guidance on the question of how soon after the contracted for date is soon enough – the sellers should be free to walk, unless the buyer expressly waives the contingency.

Editor's Comment 2: In light of the way that the clause is worded here I don't think that it is possible for a late mortgage commitment to "satisfy" the clause, because it is deemed waived if the buyer doesn't invoke it, and therefore any subsequent granting of a mortgage commitment, although useful to the buyer, has no contractual meaning.

But is it appropriate to argue generally that the seller has no duty to extend? The editor is of the view that the seller should not have the duty to extend, as this is not the sort f clause to which "time of the essence" rules ought to apply. In the particular case, however, the seller implicitly agreed to be reasonable in considering further extensions, and as a consequence the buyer did not withdraw from the contract, thus providing consideration for that consent, if any was required. (Probably no consideration is required for this sort of modification of an existing contract.)

VENDOR/PURCHASER; CONDITIONS; FINANCING: A mortgage commitment may contain conditions not contemplated by a purchase contract and still be sufficiently binding on the lender such as where the conditions are likely to be fulfilled. ***Watson v. Gerace, 175 Fed.Appx. 258, 2006 WL 839055 (3rd Cir. Ct. App. 2006); March 31, 2006.***

A contract for the sale of an apartment required the buyer to obtain a written commitment from an established mortgage lender within 19 days after the date of the contract. The mortgage commitment had to be in writing, and the loan described in the mortgage commitment had to meet certain criteria. But the clause also stated, at the end, "Any mortgage commitment signed by the BUYER will satisfy this mortgage contingency."

The buyers received a credit approval letter from an established mortgage lender within the prescribed time frame. In addition to satisfying the requirements of the contract, the credit approval letter indicated that the lender could require satisfaction from the buyers of additional criteria, including the requirement that the property appraise at an appropriate level, analysis of borrower's financial status, and verification of a second mortgage of $32,000. Apparently the second mortgage loan was to be made by the same lender making the commitment.

On the 21st day following contract execution, the sellers' broker sent a copy of the letter to the seller. The next day, the seller wrote to the buyer declaring the mortgage commitment letter unacceptable and further declaring the contract null and void. The seller filed for a declaratory judgment to affirm that the contract was null and void, and the buyer counterclaimed for damages and specific performance. Both sides moved for summary judgment. The U.S. District Court granted summary judgment for the buyer and the seller appealed.

On appeal, the Court of Appeals found first that the credit approval letter satisfied the terms of the mortgage contingency clause of the contract. Although it contained extra conditions not contemplated by the contract for sale, the District Court had found the letter to be sufficiently binding on the lender. In the Court of Appeal's opinion, the extra conditions in this case were more than likely to be fulfilled. As to the condition of the appraisal, the court implied (without actually holding) that it was inappropriate for the seller to object on the basis that an appraisal finding might conclude that the property actually was worth less than the seller had agreed to accept as a price. (That's right – they said that.)

The Court also held that while buyers under New Jersey law have the right to determine whether the mortgage contingency was satisfied, a seller does not have the same right. It reasoned that a mortgage contingency clause in a contract for sale is intended to protect the buyer, thus the right to determine the sufficiency of the commitment rests exclusively with the buyer. The court pointed out that the language stating that any mortgage signed by the buyer would satisfy the condition demonstrated that the condition in fact was for the buyer's benefit only.

As to the seller's final argument that the contract was null and void because the buyer failed to provide written notice to the seller of the credit approval letter before the deadline, the Court found that the contract language only required the buyers to obtain the mortgage commitment by the deadline. It did not require the buyer to provide notice to the seller. Although the seller arguably was entitled to demand proof of satisfaction of the condition, and did so, the original date for satisfaction of the condition did not apply to production of this proof, and indeed the sellers' withdrew from the contract after demanding and receiving the proof.

Comment 1: The result is right, but what a wretched opinion for a federal circuit court of appeals – written likely by a law clerk with no concept of real estate transactions – perhaps a graduate of a school that doesn't even bother to teach about them.

The opinion first starts with the premise that the seller did have a right to rely upon the financing clause, and then concludes that a credit approval letter subject to a variety of major uncertainties satisfied that clause. This is ridiculous. The seller wants to know that the major uncertainties concerning the buyer's right to obtain credit

have been resolved – especially the lender's review of the buyer's creditworthiness and the lender's appraisal of the property. Both things are wholly within the discretion of the lender and its appraiser. In either case, if the facts don't support the lender's making a loan, the seller will be stuck with the property off the market for a lengthy period and no sale. The purpose of the borrower relying on these clauses is precisely to prevent that from happening. The opinion suggests that in fact the borrower was creditworthy. So what? The lender didn't say so. And then there's the matter of the second mortgage loan, which apparently the lender hadn't decided to make yet. Don't get us started.

The opinion also suggests that the seller had no reason to complain if the lender should find the value deficient. Why the heck not? The seller didn't warrant the value of the property. It accepted the offer of the buyer. If the appraisal doesn't measure up in a timely fashion, and therefore a loan is not available, the seller has a legitimate interest in withdrawing from the deal. Remember that the buyer, not the seller, selects the lender that will appraise the property and make a decision to loan. The seller has every interest in wanting to know that this lender is ready to make the loan. Of course, the commitment may be subject to things changing after the commitment is made. But that wasn't the case here. The lender had barely begun its loan analysis. If the seller indeed had a right to rely on the clause, the court sold the seller short here.

Comment 2: The editor, however, agrees with the court that it was inappropriate to view this clause as intended to benefit the seller. The critical language that any loan acceptable to the borrower satisfied the condition indicated that in fact this was the buyer's condition alone. The buyer was free to waive any of the aspects of the loan described in the clause, or could rely on them to withdraw if the lender didn't commit as desired.

But for the court to say that it is a binding article of New Jersey common law that a clause can never be viewed as protecting the interests of both buyer and seller strikes the editor, again, as unnecessary and uninformed. The editor, always willing to criticize from an uninformed base himself, has not read the New Jersey cases relied upon by the court, but he suspects strongly that they are based upon individual analysis of individual contracts. The law books are full of cases finding that sellers can rely on properly worded mortgage contingency clauses, and it is highly unlikely that New Jersey common law denies sellers the right to bargain for such clauses.

VENDOR/PURCHASER; CONTRACTS OF ADHESION; ARBITRATION PROVISIONS: Developer's preprinted real estate contract was not a contract of adhesion, but provisions of the arbitration clause contained in the contract were substantively unconscionable and, therefore, unenforceable. ***State ex rel. Vincent v. Schneider, 194 S.W.3d 853 (Mo. 2006)***, discussed under the heading: "Alternative Dispute Resolution; Arbitration; Unconscionability:"

VENDOR/PURCHASER; INSTALLMENT SALES CONTRACTS; REMEDIES: Liquidated damages provision in installment sales contract not unreasonable if the potential forfeiture is only around 14% of the total contract price.***Thomas v. Scarborough, No. 2005 CA 02137 COA, 2006 WL 3290833 (Miss. Ct. App., Nov. 14, 2006).***

Thomas and the Scarborough's entered into a contact in 2001 under which Thomas, as owner of property in Rankin County, leased the property to the Scarborough's for 48 months. The Scarborough's paid $30,000, which was identified as a "Prior Equity Credit", when the contract was signed. They had the option to purchase the property at the end of the lease for $54,815. Taken together with an annual lump sum payment to Thomas and other adjustments, the total paid by the Scarborough's to Thomas would be $224,900. The contract provided in part, "If a forfeiture is enforced at the sole option of the Lessor, Lessee shall forfeit all rights and interest in and to the Property and Yshall forfeit all payments made hereunderY"

The lease payments were $1,500 per month, plus $5, 480 per year "additional rent". Lessee paid a $1.750 security deposit and agreed to pay all property taxes during the term of the lease.

The Scarborough's breached the agreement in 2004 by failing to pay rent. They vacated the premises and requested that Thomas refund the $30,000 Prior Equity Credit. Thomas refused to do so. The Scarborough's filed a *lis pendens* against the property. When Thomas went to sell the property, she agreed with the Scarborough's to escrow $22,141.57 (the $30,000 Prior Equity Credit less past due rent and other charges owed by the Scarborough's) in exchange for the release of the lis pendens.

Thomas and the title company then interpled the $22,141.57. The Scarborough's argued that the contract was ambiguous and that the contract contained an unreasonable liquidated damages provision that was unenforceable under Miss. Code Ann. § 75 2 718(1), which is part of Mississippi's version of the Uniform Commercial Code. Section 75 2 718(1) provides, "Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty."

The Chancery Court of Rankin County held that Thomas had suffered no loss since she had sold the property for a profit, and that an award of the interpleader fund to Thomas would constitute an unconscionable penalty under Section 752718(1). Thomas appealed.

The Court of Appeals, in a unanimous decision by Justice Myers, reversed and rendered judgment for Thomas. The court first determined that the contract was not ambiguous. The court then determined that Section 75 2 718(1) was the applicable standard. The Mississippi Supreme Court had used Section 75 2 718(1) as the standard for determining the enforceability of a liquidated damages provision in a contract for the purchase and sale of the land in Maxey v. Glindmeyer, 379 So. 2d 301 (Miss. 1980). In that case the court held that a forfeiture of a $75,000 down payment on a contract with a total purchase price of $150,000 was unconscionable and an unenforceable penalty. In the current case, the court noted, the $30,000 Prior Equity Credit was only approximately 14% of the total purchase price of $224,900. In comparison to the 50% penalty in the Maxey case, this was not unconscionable.

The Court of Appeals also found that the trial court had miscalculated Thomas' loss from the sale. If the Scarborough's had fulfilled their obligations under the lease and purchased the property at the end of the term, Thomas would have made a profit of $86,443. Her profit on the sale that she made was only $46,886, not including the $22,141.57. The court found it significant that the only way that Thomas would be compensated for her loss was from the interpleaded funds.

Reporter's Comment 1: These kinds of lease purchase agreements, a variation of an installment sales contract, are rarely used in Mississippi. This case illustrates why. What well-advised buyer would enter into such an agreement? The lessee/buyers in this case lost their $30,000 Prior Equity Credit / down payment and some other payments, and probably attorney's fees in trying to get their money back.

Such arrangements are fraught with other potential problems: for example, what happens if the lessor/seller dies or files bankruptcy after the lessee/buyer has made substantial payments? While undoubtedly other relevant facts exist that are not part of the published opinion, if lessee/buyers had $30,000 in cash to put down, it seems that they could have gotten a conventional home loan from a bank instead of entering into this squirrelly deal.

Reporter's Comment 2: But, given the fact that buyers did in fact enter into this contract, it's tough to make an argument that the contract that one has agreed to is unreasonable and shouldn't be enforced. It's especially hard to make that argument based on what's "reasonable" when you've breached the lease agreement by failing to make the payments that you promised to pay. In the *Maxey v. Glindmeyer* case, cited by the Court of Appeals in *Thomas*, the sales contract, prepared by an "attorney realestate broker in Milwaukee", was worldclass sloppy, and the seller and purchaser were mutually mistaken about the amount of acreage involved. Also, in the *Maxey* case, the seller did not have a subsequent sale to establish actual damages. So the equities in that case were more balanced.

Reporter's Comment 3: The editor has a knee-jerk reaction against using the UCC as a basis for filling in holes in real property law, because important principles of real property law such as title and constructive notice are generally not taken into account by the UCC. In this case, however, the most common statement of the common law rule, and one that has been used by federal courts in diversity cases applying Mississippi law – Section 356(a) of the Restatement of Contracts – is almost identical to the Mississippi version of Section 2 718(1). Section 356(a) provides, "Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in light the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty."

So at least in this case, the use of the UCC rather than the common law does not make a difference in the result.

Reporter's Comment 4: Mississippi's version of Section 2 718(1) is the same as the uniform version promulgated by the National Conference of Commissioners of Uniform State Laws and the American Law Institute prior to 2003. In 2003 NCCUSL and ALI promulgated amendments to Article 2 of the UCC. These amendments, among other things, inserted the words "and, in a consumer contract," in the first sentence of Section 2 718(1), so that the first sentence of the uniform version reads, "Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, and, in a consumer contract, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy." The 2003 amendments also drop the last sentence of Section 2 718(1), which provides, "A term fixing unreasonably large liquidated damages is void as a penalty." However, Mississippi has not adopted the 2003 amendments to Article 2. In fact, the editor's quick research suggests that no state has adopted the 2003 amendments. What's up with this?

Editor's Comment: In the world of installment land contract remedies, and mortgage remedies in general, there's really nothing unusual about a borrower arguing that the lender's remedies are overreaching. The whole basis for the creation of the equity of redemption is that real estate purchasers frequently do not focus clearly on the remedies section of the agreement, while lenders and sellers do – leading to an inherent imbalance in bargaining. Throughout the country, courts routinely set aside forfeitures in installment land contracts in a wide range of circumstances. In fact, outside of a few states – Minnesota, Michigan, and possibly New Mexico, to name a few, enforcement of installment land contracts as written is hardly the norm – it is the exception.
The editor read the original version of this case, and admits to a great deal of frustration in the court's opinion. It does not tell us the relationship between the apparently hefty "rental" payments and the market rent. (The credit that the seller took in the agreement to escrow the $30,000 included claims for accrued but unpaid "additional rent" plus an amount for some unpaid property taxes.) It does not tell us why it was a reasonable "liquidated damages" agreement for the seller to take a $1,750 "security deposit" when it already had a forfeitable $30,000. It does not tell us the price that the seller received for the property on resale, nor the method by which it computed the profit (did it count all the "rental" payments as payments on the price? Even "effective interest" components?) It also does not tell us why the lower court figured the profit differently.

In short, what we have is a virtually unintelligible piece of precedent that will mislead and confuse trial court judges while contributing nothing to a workable approach to this difficult and controversial real estate device. Not what the editor has come to expect from Mississippi, where you always get a good story and often some reasonably sound analysis.

The reporter for this case was Rod Clement of the Jackson, Mississippi, Bar. .

VENDOR/PURCHASER; LEASE OPTION; EXERCISE: Where purchaser deposits substantial cash payment at outset of lease option period, and purchaser's "rent" thereafter corresponds closely to the varying payments on seller's underlying mortgage, purchaser may be viewed as having already exercised option, even though he dies nine years later without having formally exercised the option. ***Lee v. Bass, 2007 Westlaw 505386 (2/20/07) (opinion not yet finally approved for publication)***

The parties, personal friends, negotiated the sale of a home without benefit of counsel or anyone else who knew much about the law. Lee was to purchase the house from Basses. They originally agreed upon a standard purchase and sale agreement, selling the home for $84,500 subject to a mortgage of about $71,500. They then came to realize that a due on sale clause in the existing mortgage would preclude the buyer from taking advantage of the payment terms under the existing loan. They elected instead to do a "do it yourself" lease option arrangement, which they believed would permit them to circumvent the due on sale clause. They therefore disregarded the already negotiated purchase and sale agreement.

The parties got a lease form from a stationery store and one of the sellers used that as the basis for their agreement. The final version stated that Lee would make payments equal the Bass' mortgage and escrow obligations. At one point in the contract, these payments were identified as rent, but at another point, the parties, in discussing the payments, crossed out language in the

form document referring to them as "rent". The arrangement otherwise was set up as a lease, including a landlord's termination right for tenant's failure to perform, except that the option provision indicated that if Lee had an option to purchase within one year, and if he did, the purchase price would be $84,500 and Lee would pay $13,000 in cash as a "down payment". There is no indication in the agreement whether Lee was expected to pay the balance of the price in cash. Further, although the agreement apparently doesn't so require, Lee paid all expenses and taxes.

Lee in fact paid the $13,000 immediately upon signing the lease/option contract, a few days before taking possession, but there were no further actions taken to effect a closing. There was no assumption of the existing mortgage, no deed delivery, nothing. Lee remained in possession and made rent payments for nine years. Although the lease stated that Lee would pay about $690 per month in payments, in fact whenever the Bass' mortgage payment went up, Lee made a larger monthly payment. Then Lee died at age 57.

The Bass' had treated the property for that nine years as rental property, taking depreciation deductions and treating the mortgage interest as an expense. We don't know how they treated the $13,000. Lee treated the deal as a purchase for tax purposes, and treated the contract as a wrap- around mortgage, deducting the interest component of the payments as home mortgage interest.

Lee's heirs attempted to perform the contract by tendering the balance of the purchase price, and the Bass' refused to perform. By their analysis, Lee had failed to exercise the option in the first year provided for in their agreement, and thereafter they were "nice enough" to permit Lee to live in the property as a tenant, an arrangement they were free to terminate on one rent period's notice. (It should be noted that there had never been any default by Lee in any of his obligations.)

The Bass' characterized the $13,000 payment as consideration for the option, to be credited to the option price if the option were ever exercised. The trial court bought their argument and refused to grant specific performance.

The Missouri Court of Appeals reversed. It noted that the parties had never indicated in their agreement that the $13,000 was consideration for receiving the option, but rather that the payment of the $13,000 was to be made in connection with exercise of the option. In short, in the view of the appeals court, Lee exercised the option on the day the contract was signed, and the parties were very, very delinquent in carrying out the other elements of their arrangement.

Comment 1: The court reached the right result, but it is a little silly to try to treat the efforts of these parties as a bona fide real estate arrangement. It was a complete mess. In most cases, a contract that calls for a purchase of property subject to a mortgage and does not indicate whether the buyer is obligated to assume the mortgage, pay it off, or merely take "subject to", might be regarded as unenforceable because it is impossibly vague (Of course, the buyer may avoid that defect by paying cash, as apparently the heirs were willing to do here.)

The court makes nothing of the fact that the Bass' treated the property as a lease from the start. Although they in fact did raise the "rent" that Lee paid whenever their payments went up, they did not lower the amount when their payments went down, such as they did when the Bass' refinanced. That's right – the Basses refinanced in the middle of what the court regards as a postponed closing of an already agreed upon sale.

In short, what the court did is impose order on chaos.

Comment 2: Note that what the parties did would not, of course, have avoided the due on sale clause in a standard mortgage. It might have prevented the lender from discovering the sale, but a lease with an option to purchase almost certainly is the "transfer of an interest" within the meaning of the standard clause.

VENDOR/PURCHASER; TITLE; "INSURABLE TITLE": A purchaser of a condominium unit is entitled to the return of a down payment when the title company will not insure title to the unit due to the condominium board's imposition of a condition it had no right to impose. ***Lisenenkov v. Kaszirer*, *827 N.Y.S.2d 579 (Supp. 2006*)**

Purchaser entered into a purchase and sale contract that required seller to deliver insurable title to the condominium unit. The title company refused to remove as an exception from title the condominium board's right of first refusal unless the board certified that it did not possess such a right. Although the condominium board

did not have a right of first refusal, the board refused to provide the required documentation to the title company until the purchaser paid $20,310.72 as an advance of 2 years of future common charges. The Court found that the condominium board did not have the right to impose such a condition on delivery of the certification and as a result the purchaser was under no legal obligation to pay the advance. The condominium's board refusal prevented the seller from delivering insurable title to the purchaser, which was a condition precedent to closing. Therefore, the court held that the purchaser was entitled to the return of her deposit.

VENDOR/PURCHASER; SPECIFIC PERFORMANCE; USURIOUS INTEREST RATE: Court did not err in awarding specific performance of the remaining provisions of a lease containing an option to purchase the property at a usurious interest rate, and tenant did not waive the issue of usury by seeking specific performance. ***Van Carr Enter. v. Hamco, Inc.,2006 WL 649985 (Ark. 3/15/06)***

Landlord and tenant entered into a fixed term commercial lease agreement with an option to purchase the building, which could be exercised at any time during the period of the lease. If tenant elected to purchase the building, landlord agreed to finance the purchase at an interest rate of 7% for 5 years and thereafter at 6% above the Federal Discount Rate (FDR) for 15 years. On the date of the lease, the FDR was 1.25%.

Article 19, Section 13 of the Arkansas Constitution provides that the maximum lawful rate of interest on any contract cannot exceed 5% above the FDR at the time of the contract, and any contracts having a rate of interest in excess of the maximum lawful rate shall be void as to the unpaid interest.

Tenant filed suit alleging breach of contract and seeking specific performance under the lease. Landlord countered that the contract contained an unlawful rate of interest and was illegal on its face. The circuit court declared that the interest rate under the contract was usurious and void but awarded specific performance of the remaining provisions of the contract and voided the remaining leases. On appeal, the Supreme Court affirmed the circuit court's decision and rejected landlord's argument that tenant should be estopped from asserting that the interest rate in the contract was usurious because tenant waived the issue by seeking specific performance of the contract. The Court reasoned that because the contract at issue is void as to the unpaid interest under Arkansas law, a borrower cannot waive a usury defense by simply requesting specific performance of the remaining clauses of the contract.

Comment 1: The editor found interesting the court's willingness to let the contract go forward despite the significant change in the return to the seller based upon the usury finding. But that's usury law – very severe, and therefore to be avoided if at all possible.

Comment 2: The editor also found interesting the court's failure to apply the "time price doctrine", which states that a seller can charge a different price for payment over time, even if the price is expressed as composing both principle and interest, and still the payment is a payment for the thing sold, and not for a loan of money or an advance of credit. Consequently, under this doctrine, usury laws do not apply to seller financing. Apparently Arkansas, under its constitutional usury provisions, has decided not to follow that law.

VENDOR/PURCHASER; "TIME OF ESSENCE": A purchaser's untimely tender of an interim payment in a sales contract without a "time of the essence" clause does not constitute a material breach of the contract, and use of the phrase "in no event later than" a specified date, does not make timely performance "of the essence". ***ADC Orange, Inc. v. Coyote Acres, Inc. 824 N.Y.S.2d 192 (Ct. App. 2006)***. ADC Orange entered into a sales contract with Coyote Acres to purchase a parcel of real property. The contract required that ADC Orange make an interim payment of $250,000.00 no later than December 31, 2001. The interim payment in fact was made on January 11, 2002, at which time Coyote Acres declared that ADC Orange was in default. ADC Orange brought an action for specific performance of the sales contract. The court noted that the contract did not contain an express "time of the essence clause" and the court found that using "in no event later than" did not make December 31, 2001 of the essence. Without a time of the essence clause, ADC Orange had a reasonable time in which to make the interim payment and was not in material breach of the contract.

WHARFS AND DOCKS; "PROPERTY": Floating docks are not real property within the meaning of casualty insurance policy. ***American Home Assurance Co. v. AGM Marine Contractors, Inc., 467 F.3d. 810 (1st Cir. 2006).***

The Town of Provincetown contracted with the defendants to construct a pier and install a floating dock system. The entire dock system was destroyed in a storm and AGM Marine Contractors, Inc. filed a claim with the plaintiffs. The plaintiffs denied the claim for coverage and filed a petition for declaratory judgment, and the United States District Court for the District of Massachusetts granted summary judgment in favor of American Home Assurance Co. The holding that came out of this case is that in Massachusetts, floating docks are not real property. According to the Court, case law in other jurisdictions is divided. The rational for excluding floating docks from the definition of property is that floating docks can be removed from the land without damage to the land. Further, the affixation to the land was not an alteration of their character as chattels. They were attached to the land only to steady them for more convenient use.

WORDS AND PHRASES; "REAL PROPERTY": FLOATING DOCKS: Floating docks are not real property within the meaning of casualty insurance policy. ***American Home Assurance Co. v. AGM Marine Contractors, Inc., 467 F.3d. 810 (1st Cir. 2006),*** discussed under the heading: "Wharfs and Docks; 'Property'."

ZONING AND LAND USE; "FAIR SHARE" ZONING; HOUSING: An administrative agency, particularly one entrusted to fulfill government affordable housing obligations, has wide discretion in selecting the means by which it fulfills its delegated duties, and a reviewing court should normally defer to that choice so long as the selection is responsive to the purpose and function of the agency. ***In Re Adoption of Uniform Housing Affordability Controls, 390 N.J. Super. 89, 914 A.2d 402 (App. Div. 2007); January 25, 2007.***

Under New Jersey's Fair Housing Act (FHA), municipalities must provide a realistic opportunity for the construction of lower-income housing for qualifying individuals. This law was enacted in recognition of the *Mt. Laurel* case decisions that recognized such an individual right was rooted in the New Jersey Constitution. To implement the *Mt. Laurel* doctrine, the FHA created the New Jersey Council on Affordable Housing (COAH) to provide an administrative mechanism for implementing the doctrine. The FHA directed COAH to adopt criteria and guidelines that would enable a municipality to determine its fair share of its region's present and prospective housing needs. To implement its mandate, COAH developed regulations. COAH ultimately adopted Uniform Housing Affordability Controls (UHAC) as part of its overall regulatory structure. In addition, other agencies such as the New Jersey Housing and Mortgage Finance Agency (HMFA), adopted UHAC. UHAC rules were aimed to ensure that affordable housing units, restricted to persons with low or moderate incomes, would remain occupied by persons meeting those income levels. Affordability averages were designed. These represented the percentage of median income at which restricted units in an affordable development were affordable to low and moderate income households. The averages stated that municipal ordinances were to require that the average rent for low and moderate income units be affordable to households earning no more than 52 percent of median income, and that an affordable development must achieve an affordability average of 55 percent for restricted ownership units.

An affordable housing advocate filed a suit challenging these calculations, specifically as to HMFA's methodology. The advocate argued that HMFA's affordability ranges excluded housing opportunities for lower-income households. The Appellate Division first noted that courts normally defer to the discretion of an administrative agency in fulfilling the duties of the legislature, and such deference is more particularly applicable when reviewing administrative regulations adopted by COAH in furtherance of the FHA. The Court held that the FHA vests COAH with primary jurisdiction over the administration of these housing obligations, and HMFA's role is to complement, not supersede, COAH's interpretation and implementation of the *Mt. Laurel* doctrine. The Court, referring to public comment at the time of the proposed adoption of UHAC, noted that COAH had considered, but rejected, a lower ceiling because of realities in the marketplace. In reaching that conclusion, COAH relied upon the experience and expertise of affordable housing finance professionals. The Court stated that it was not the court's role to second-guess that choice, especially when the advocate presented no studies or analyses that would mandate a different result.

The Court concluded that the advocate failed to meet its burden that the HMFA regulation being challenged was inconsistent with its legislative mandate. It found that the

affordability ranges enacted reached low income households. That it did not reach more low income households did not render the regulation invalid. Accordingly, the Court could not conclude that the agency clearly erred or violated statutory or constitutional provisions.

ZONING AND LAND USE; REDEVELOPMENT; BLIGHT: The New Jersey Constitution does not permit government redevelopment of private property solely because the property is not used in an optimal manner. ***Gallenthin Realty Development, Inc. v. Borough of Paulsboro, 2007 WL 1687274 (N.J. Supr. Ct. 2007 6/13/07).***

A municipality was bounded by a river and was bisected by a railroad freight line that divided the municipality into two neighborhoods. The southern neighborhood contained most of the older residential development. The northern neighborhood extended from the river to the railroad, and contained housing and industrial development.

There was a vacant parcel adjacent to the river. Its owners listed it for sale as suitable for the operation of a dredge deposit site. The property was permitted to accept United States Army Corp of Engineer's dredged material, but had not been used for such purpose since 1963. The property owners requested rezoning of the property from manufacturing (M) to Marina Industrial Business Park (MIBP), which would allow a variety of mixed non-residential, commercial, and light industrial uses. The municipality made the change.

Some time later, the municipal governing body adopted a resolution authorizing the planning board to conduct a preliminary investigation to determine whether the designated parcels, including the subject property, met the statutory criteria for designation as areas in need of redevelopment. The investigation recommended inclusion of these parcels, including the subject property, within the area in need of redevelopment in the master plan as well as their inclusion in the municipality's redevelopment plan.

The planning board scheduled a public hearing to determine the need for redevelopment and revitalization of the parcels in the redevelopment plan. The board's professional planner presented the matter to the planning board. He stated that he had conducted a site inspection and he displayed photographs of the subject property noting that the property lacked physical improvements of any type. The planner concluded that the property's condition constituted "economic deterioration". He suggested to the board that if the property was improved in conjunction with the redevelopment plan, the aggregate result would be beneficial to the municipality. The planner further stated that the condition of the subject property satisfied the statutory criteria of: a growing lack or total lack of proper utilization of areas resulting in a stagnant or not fully productive condition of land potentially useful and valuable for contributing to and serving the public health, safety, and welfare.

The property's owners introduced a professional planner who testified that the property did not meet the redevelopment criteria set forth in the pertinent statutory provision because the property owners were in the process of undertaking development activity on the site. The planner testified that the planning board's planner failed to consider the historical use of the property as a dredge disposal site and its availability for such use. However, the property owners' planner also admitted the property had not been used as a dredge site for over 40 years and that there were no current permits for such use. Nonetheless, based on the actual or potential activities on the site, the planner concluded that property owners' property did not meet the redevelopment criteria.

The property owners also testified and provided a detailed history of the property. They outlined their plans for development as a dredge deposit site. They also explained that the property had been farmed for approximately the last seven years, although they admitted that little economic benefit had been derived from that farming activity.

At the conclusion of the hearing, the planning board voted unanimously to reject the testimony of the property owners' planner and approved the recommendation of the planning board's engineers that the subject property was an area in need of redevelopment. The planning board then adopted a resolution finding that the subject property constituted an area in need of redevelopment for the reasons expressed in the report of the planning board engineers and the reasons stated in the testimony of the planning board planner at the hearing. The governing body adopted a resolution approving the recommendation of the planning board. It then enacted an ordinance adopting the redevelopment plan that incorporated the subject property.

The property owners filed a lawsuit alleging that various municipal officials conspired to use the redevelopment statute to deprive them of the their development rights to the property, that the master plan did not include the subject property as an area in need of rehabilitation, that there were various substantive and procedural flaws in the procedures employed, that the planning board's attorney was in conflict of interest, and the subject property did not meet any of the criteria set forth in the pertinent statutory provision. Following hearings, the lower court dismissed the complaint.

The property owners appealed. To their consternation, the Appellate Division found that there was substantial evidence supporting the governing body's determination that the subject property was an area in need of redevelopment pursuant to the criteria set forth under New Jersey's enabling statute, the Local Redevelopment and Housing Law (LRHL). The disappointed property owners appealed further, this time to the New Jersey Supreme Court, attacking the municipality's designation of their land as being "in need of redevelopment" on constitutional grounds.

Here, the appeal succeeded. According to the New Jersey Supreme Court, the New Jersey municipalities must read the statutory definition of "blight" in the LRHL very narrowly so as to comport with the Constitutional language authorizing condemnation for that purpose.

> "[t]he [New Jersey] Constitution expressly authorizes municipalities to engage in redevelopment of 'blighted areas'. The State may take private property only for a 'public use'. Under the blighted areas clause of the New Jersey Constitution, the clearance, replanning, development, or redevelopment of blighted areas shall be a public purpose and public use for which private property may be taken or acquired."

The Court reviewed the history of the Constitution's "blighted areas clause" as adopted in 1947 and concluded that "the framers were concerned with addressing the deterioration of certain sections of older cities that were causing an economic domino effect devastating surrounding properties." Consequently, the Constitution was drafted to enable municipalities "to intervene, stop further economic degradation, and provide incentives for economic investment."

With that in mind, the Court felt that the essential issue in this dispute was the definition of the word "blight" as used within the Constitution. It concluded that "[a]lthough the meaning of 'blight' has evolved, the term retain[ed] its essential characteristic: deterioration or stagnation that negatively affects surrounding properties."

In contrast, the LRHL arguably interpreted the Constitution's use of the term "blight" to refer to "any property that is 'stagnant or not fully productive' yet potentially valuable for 'contributing to and serving' the general welfare." The Court rejected this "all-encompassing definition", finding that if this were the meaning intended under the Constitution, "most property in the State would be eligible for redevelopment."

Based on its analysis, the Court held that the Legislature could never have intended that the LRHL would function in other than a constitutional manner. Consequently, the Court held that the power granted to a municipality to condemn property "in need of development" could only apply to "property that has become stagnant because of issues of title, diversity of ownership, or similar conditions." Interpreting the LRHL in that fashion, the Court avoided rendering the statute or its challenged part unconstitutional while still "giv[ing] effect to the Legislature's original purpose in adopting the language" that became the basis for the statutory scheme granting municipalities broad redevelopment powers over "blighted" properties.

As a result of this holding, the municipality's designation of the property in question as being "in need of redevelopment" was set aside, without prejudice to "any future inquiry" by the municipality "regarding whether the property is 'in need of redevelopment' based on any other legitimate grounds."

Editor's Comment: What a torturous way to get a Constitutional reading of an unconstitutional statute. Clearly the court expects that the legislature is paying attention and that it will revise the language of the LRHL. Otherwise, other municipalities also will read the statute in accordance with its apparent meaning (rather than its narrow, "constitutional" one) and also violate unconstitutionally deprive citizens of their property rights.

Editor's Comment 2: Also see: ***Centene Plaza Redevelopment Corp. V. Mnt Properties, 2007 WL 1695153***

(June 12, 2007), discussed under the heading: "Eminent Domain; Urban Renewal; 'Blight'." A determination of blight for purposes of a condemnation by a redevelopment corporation in Missouri must be based on evidence of both economic and social liabilities in the project area; economic liabilities alone are not sufficient.

The reporter for this item was Ira Meislick of the New Jersey bar. The editor did his thing.

ZONING AND LAND USE; RELIGIOUS ACTIVITIES; RLUIPA: To demonstrate burden religious activities that government zoning officials must accommodate, applicant may simply demonstrate that alternative properties with property zoning are not available to it because it lacks adequate financial resources. ***Shepherd Montessori v. Anne Arbor Charter Township, 2007 WL 1486138 (Mich. App. 5/22/07)***

Applicant, which apparently has some affiliation with the Ave Maria Foundation, a religiously oriented nonprofit foundation with considerable resources, sought to obtain a variance to operate a Montessori primary school adjacent its existing day care facility. The subject property was within the Domino's Industrial park, and the zoning for the Park permitted day care centers within the zoning district, but only to serve employees of businesses operating within the district. The Township, however, had earlier granted a variance to another day care operator, "Rainbow Rascals", to operate on the site a day care facility substantially larger than that proposed by applicants.

The applicant applied for a variance, noting that the impact of its use would be far less than that of "Rainbow Rascals", as it would have only one quarter the number of students, and that the proximity to the existing day care facility enabled it to make use of the chapel on that facility, which was vital to its religious education mission. The zoning authorities refused the variance and this action ensued, alleging both RLUIPA and Equal Protection Clause violations.

The trial court granted summary disposition to the defendant Township, and that case had been reversed and remanded by the court of appeals, instructing the trial court to determined whether the denial of the zoning variance placed a significant burden on plaintiff's religious activities and to address (1) whether there were alternative locations that would allow the school consistent with the zoning laws; (2) the actual availability of alternative property, by sale or lease, within the area; (3) the availability of property that would be suitable for a K-3 school; (4) the proximity of the homes of parents who would send their children to the school; and (5) the economic burdens of alternative locations. The Michigan Supreme Court denied an appeal from the Appeals Court's remand.

On remand, the trial court, at least according to the view of the current appeals court panel, chose not to believe the evidence supplied by the plaintiffs, even though the defendants made scant effort to refute it, and granted summary judgment again for the Township. Critical to the trial court's ruling was that it viewed the evidence of what the plaintiff could afford as essentially self serving. It noted that other cases elsewhere had held that a RLUIPA claim cannot be based upon the claimed lack of funding of a religious institution to support its activities elsewhere because the institution is in complete control of its estimate not only of costs but of probable revenues and other funding. The court apparently was of the view, and the Township strongly argued, that the close ties between the plaintiff and the Ave Maria Foundation meant that it had access to extensive financial resources.

The Appeals Court this time spanked the trial court hard. It criticized the court for looking to authority from other jurisdictions when the law of the case, established by its prior ruling and other rulings it had made, was that the subjectively reported financial ability of the applicant to acquire other properties and operate its activities was relevant to a RLUIPA claim. It indicated that there was no evidence in the record of any commitment or contract from the Ave Maria Foundation or any other funding source – in fact quite the contrary, as the Foundation had indicated it had no plans to fund the school. The appeals court not only overturned summary judgment for the Township, it found that the trial court should have granted summary judgment for the plaintiff on *both* the RLUIPA claim and the Equal Protection Clause claim (do we smell a 1983 claim for the costs of this litigation in the wind?)

Importantly, the court ruled that it is not necessary for an RLUIPA claim to show that the property in question is essential to the plaintiff's proposed religious activity – but only to show that the denial of the requested zoning relief would place a burden on that activity. That would arise, of course, if the plaintiff could show that it could not afford to conduct its proposed activity anywhere else

convenient. Note that since plaintiff already owned the subject property, its costs in using that property would be substantially lower than comparable sites.

The trial court had elected not to credit the comments by plaintiff that it could not afford the other sites, commenting:

> "Courts have held with good reason that inconvenience and/or high cost of real property in a particular area should not suffice to establish a substantial burden . . . It will always be relatively easy for a plaintiff, such as [plaintiff], to articulate some ostensibly logical reasons for rejecting any property but the property in dispute."

Whoops – said the appeals court. We specifically told you on remand to consider plaintiff's evidence about comparable sites. And now we find that evidence was substantial and credible and inadequately refuted by the Township.

Comment 1: Somehow lost in all of this was the fact that we had a primary school, not a day care center, applying for a variance. The Township apparently loaded all its ammunition in establishing that there was inadequate basis for the religious claim, and made no serious effort to show that its zoning objectives in denying primary schools at this location would be compromised. The fact that the Township had earlier permitted a facility caring for 100 kids was too much for the appeals court to ignore when the applicant, wanting to care for only 25 kids, albeit a little bigger kids, came in. The traffic and other impacts, of course, were going to be substantially less.

Comment 2: This did seem to be a pretty dumb case for the Township to blow its litigation budget on. Maybe the trial court did detect some religious animus here. The more the Township litigated, the more hollow its nondiscrimination claim became. There clearly was something personal going on here.

Comment 3: Nonetheless, the case does establish a proposition that a RLUIPA case will be pretty easy to make where the applicant has a low land cost (perhaps because of donated land) and proposes a use that works with cheap land and doesn't work otherwise without other institutional support. The court apparently will not be able to take into account the likelihood of that institutional support, at least not when there is no prior history of such support. And eliminating prior history is no more difficult that setting up a new entity to conduct the proposed use.