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Sponsor:
Section of Real Property
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Editorial Contributor:
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Quarterly Report on Current Developments in Real Estate Law

January 1, 2007 through March 31, 2007

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ATTORNEY'S FEES; SPECIFIC PERFORMANCE: A court may not permit a successful buyer in a specific performance action to credit the attorney's fee award against the buyer's obligation to pay the purchase price. ***Behniwal v Mix 147 CA4th 621, 54 CR3d 427 (2007),***discussed under the heading: "Vendor/Purchaser; Specific Performance; Attorney's Fees."

BANKRUPTCY; HOMESTEAD: A Chapter 7 bankruptcy debtor may claim the homestead exemption where the real property was transferred to a revocable trust prior to the bankruptcy and the bankruptcy debtor was both the settlor and a beneficiary of the trust. ***Redmond v. Kester, 2007 WL 1649931 (June 8, 2007),*** discussed under the heading: "Homesteads; Transfer to Trust; Homestead Exemption; Title Insurance."

BROKERS; BUYER'S BROKERS; DUAL REPRESENTATION: Where statute imposes a duty upon buyer's broker to work "solely in the best interests of the buyer," broker may not present offers from two buyers to the same seller, but must direct at least one of the buyers to another agent for purposes of presenting the offer. ***Zuazua v. Tibbles, 150 P.2d 361 (Mont. 2006)***

Virtually all the discussion in this case is based upon interpretation of the operative agency legislation. Undoubtedly this legislation originally was lobbied through by the Montana Association of Realtors and undoubtedly a legislative "fix" is either completed or well on its way by now. But it still it is useful to review the concepts at work in this area and to think again about the function of a buyer's broker and what the Realtors are doing to themselves here.

Stone, an agent of the Coldwell Banker agency, had on July 8 executed a form with Zuazua that identified Stone as a buyer's agent for Zuazua. Two days later, Zuazua authorized Stone to submit an offer on a property. Two days after that, Stone signed another buyer's agency agreement with Moritzky and submitted an offer on the same property on that same day. Even though two days had passed since the supposed presentation of the first offer, the seller testified that he evaluated both offers and accepted Moritzky's.

Zuazua sued in federal court, and the court referred to the Montana court the question of whether the Montana statute prohibits a buyer's agent from submitting two offers from two different clients on the same property. Apparently there was a lot more allegedly going on than this one little behavior, but we are fortunately spared the messy details and permitted to look only at this isolated issue of statutory interpretation.

As indicated, the Montana Supreme Court, in a split decision, found that the requirement in the statute that the buyer's broker work "solely in the best interests of the buyer" was dispositive of the question, and it ignored other language, emphasized heavily by the three dissenters, that implicitly authorized buyer's brokers to submit offers from different brokers, subject to the injunction that the broker could not disclose to either client the terms of the other bid. The Montana Real Estate Commission had already issued rules permitting the submission of competing offers by the same agent. Both sides agreed that the statute did not expressly address the practice.

The Supreme Court limited its decision to the behavior of the individual agent, and would have permitted the agent in question to designate (with client consent) another agent in the same office to move forward on an offer. Indeed, one commentator on the case suggested that, if the result stands, agents might be well advised to designate different "submitters" for each of the buyers, so that the designated buyer's agent can maintain comfortable relations with both buyer clients after the issue is resolved. (Remember that the seller might reject both offers, leaving both clients still looking.)

Comment 1: As indicated above, in many states it appears that the NAR lobbying machine can get pretty much what it wants out the legislators. Who's to oppose them? The class of consumer customers is too diverse and constantly changing. In any event, the NAR can fill the air with expertise backed arguments that make anything the lobbyists want sound just like delivery of Mother's Apple Pie to the deserving consumer clients. So, as a legal matter, it is likely that the brokers ultimately will get what they want. And what they want here obviously increases the return to an individual agent (who won't have to share commissions or pay fees to buddies) and maintains the ability of the agent to control the deal – always a good thing.

Comment 2: The brokers argue that they will still be required to disclose to their customers what they are doing, so everything is just fine. Really? The disclosure will be in a tightly written form provided at the outset of the representation, and every other candidate for buyer's agency (assuming that in fact the agent is incompetent enough to let the customer out of his or her clutches in order to shop around) will present the same "official" form. It takes a sophisticated buyer indeed to fight back on these forms, and in practice there is very little "give" from brokers in the residential marketplace even if they do. In any event, the customer has only the agent in front of him or her to explain where the problems lie in that form. Clearly any acceptance of the terms can hardly be regarded as fully informed.

Comment 3: Apparently, the Montana Association of Realtors, at argument, took the position that the individual buyer clients' interests are not at stake in the dual offer situation because the buyer's broker plays little function in the presentation of the offer, and thus neither client's position can be adversely affected? Oh yeah??? If that is so in Montana, then brokers there have abdicated an important function for which, allegedly, they are being paid. From the buyer's standpoint, probably no function of their agent is more important than the agent's function as a "closer" – to be present at the presentation of the offer, to calculate the seller's response to its terms, and to advocate for acceptance or identify subtle changes that might bring the seller around to the buyer's position. But if there is more than one buyer, which one is entitled to the agent's persuasive talents? Clearly the maximum benefit can be provided when the agent is representing only one interest.

Comment 4: This gets the editor around to his favorite rant – one which he directs at his own brethren in the bar as well as at the brokers: What happened to professionalism? It seems that at every turn in the development of ethical standards, the skilled professions are advocating for positions that make their economic return higher and the level of professional service lower. In fact, it might be said that the positions make it possible for huge, multi purpose offices to take such a bewildering array of positions that they can be all things to all people, and extract money in every instance. The concept of the individual agent providing personal expertise and loyalty to the individual client is lost in the shuffle.

Those advocating these positions may take the position that the vast majority of clients are better served at lower costs through mega firms and standardized positions, and that personal service never really existed before – it was only represented to exist – and that the "one size fits all" approach truly is best suited for the modern era.

The problem with this approach is it tends to undercut the very rationale for the existence of licensed monopolies for these service providers – that a high level of skill and judgment is required in order to provide the services in question, and that therefore there should be a professional class established with barriers to admission, so that the public can be assured that it is receiving the necessary skills.

Without the rationale that individual skill and high levels of loyalty are fundamental to representation of professional clients, there is scant argument for the regulated monopoly that we create for our brokers and lawyers. Rant ended. Let it be recorded, at least, in the history.

Comment 5: The editor takes no position on what the law ought to be for commercial brokers. In general, he believes that there is more of a true market in this area, and regulation of residential brokerage and commercial brokerage are two different things and ought to be so regarded by the NAR. Unfortunately, the politics in most states are such that the commercial brokers must ride the coattails of the legislative efforts of the residential side, which has all the power in the local associations. Another sad reality. The editor has no notion as to whether it is inevitable, or simply convenient.

BROKERS; LEASING BROKERS; COMMISSION: A broker was not entitled to its commission in a failed real estate transaction where, following a dispute, the parties settled their claim with tenant paying a substantial settlement and the lease being cancelled. No commission was payable because a condition precedent to the landlord's obligation to pay the commission, namely the tenant's payment of "rent," never occurred. ***HGCD Retail Serv. v. 44-45 Broadway Realty, 826 N.Y.S. 2d (A.D. 1 Dept. 2006).***

Landlord entered into a brokerage agreement with a broker whereby landlord agreed to pay the broker a commission of approximately $1.4 million, the first quarter due after all commission payment conditions were satisfied and the remainder payable in eighteen equal installments, commencing after the tenant makes a rent payment other than the first month's rent due upon execution of the lease. The commission payment conditions include: (i) execution and delivery of the lease, (ii) landlord's delivery of possession of the leased premises to the tenant and (iii) that tenant is not in default in the payment of rent.

After the lease was executed, an issue arose as to whether landlord delivered to tenant possession of the premises. Both landlord and tenant commenced lawsuits against each other, the tenant claiming that the landlord had failed to complete the landlord's work and the landlord alleged that the tenant failed to pay rent when due. Both actions were settled and as a part of the settlement, the tenant paid the landlord $8.75 million and the lease was terminated.

Two months later, the broker sent the landlord an invoice for its commission and when the landlord replied that no commission was due, the broker commenced the present action. The court found that the unequivocal language of the brokerage agreement conditioned payment of the balance of the commission on the tenant's payment of rent. The court noted that although the tenant's payment of rent was not a commission payment condition, it was nonetheless a condition precedent to the landlord's obligation to pay the first quarter of brokerage commission because ignoring this condition, would undermine the fact that the balance of the commission was only due once rent was paid.

In addition, the tenant's settlement payment neither satisfied tenant's obligation to pay rent nor eliminated its obligation to pay rent. As a result, the court held that the broker was not entitled to its commission.

Comment 1: One supposes that the broker would have the right (unless now collaterally estopped) to litigate the issue of whether the landlord in fact breached the agreement and gave the tenant the right to walk out of the agreement, thus depriving the broker of the commission. But without the involvement of the tenant, such an enterprise certainly would be expensive and high risk.

Comment 2: It would be difficult for the broker to draft around this eventuality, since likely the landlord would stick to the position that no matter how large the settlement, if the landlord doesn't get a lease obligating the tenant to pay rent for the term, the broker ought not to be compensated. The landlord has a point, of course, if in fact (as the landlord would maintain here) it was the tenant that in fact was in default and spoiled the deal.

Comment 3: Although there is no formal commission payable here, is there *quantum meruit* for whatever amount the settlement exceeded landlord's costs in dealing with the problem? In other words, should broker be compensated to the extent that the settlement represented landlord's lost expectation of rent? Why not?

CONSTITUTIONAL LAW; DUE PROCESS; TAKINGS; REGULATORY TAKINGS: City's requiring connection of all new construction to city's broadband telecommunications system is an unconstitutional taking. ***Home Builders Ass'n v. City of Lebanon, 854 N.E.2d 1097 (Ohio App. 12 Dist. 2006), appeal den'd 854 N.E. 2d 1097 (8/2/06).***

The City of Lebanon (the "City") constructed a broadband telecommunications system (the "System") to which homeowners could subscribe for computer, television or telephone communications. To connect to the service, the City would wire from the public right-of-way, across the private property to the exterior wall of the structure. Initially, the City also used the System for automated electric meter reading to approximately 200 homes but determined the service was too costly to install to additional homes.

In 2002, the City adopted an ordinance requiring all new construction to connect to the System and to pay a telecommunications connection fee (the "Ordinance"). In June 2002, Home Builder's groups challenged the Ordinance on three major claims: (1) mandated connection to the System constituted a taking without just compensation; (2) the city's action constituted abuse of the city's corporate power; and (3) the ordinance violated the Homebuilders constitutional rights under Section 1983. The Homebuilders a sought a declaratory judgment that the Ordinance was unconstitutional, preliminary and permanent injunction prohibiting the city from enforcing the ordinance and attorneys' fees.

The common pleas court ruled for the Homebuilders on the first claim – that the mandatory connection did constitute an unconstitutional taking. The court, however, found that the fee was enforceable provided that it was charged only to those requesting access to the System. On the second two claims, the common pleas court found for the City because the Homebuilders did not have taxpayer standing under the state law corporate action claim, and with regard to the Section 1983 claim, had not exhausted state law remedies.

The court dismissed all remaining claims of the parties, and the Homebuilders and the City appealed to the Court of Appeals of Ohio Twelfth District (the "Court").

On the first claim of mandatory connection, the City in fact admitting that the extension of the connecting wire could constitute a taking under *Loretto v. Teleprompter Manhattan CATV Corp* 458 U.S. 419 (1982), but claimed that the Homebuilders effectively consented to the requirement when they requested electrical service and agreed to abide by the rules of the City's electric department. The Court found that even though the wires are a small invasion, under *Loretto* any permanent occupation for which just compensation is not paid constitutes an unconstitutional taking. The Court found the Homebuilders did not consent because the City was using the System to read meters in only approximately 200 homes and the hope to use the System in the future was insufficient to find consent. In short, consent to electrical service was not consent to a hook-up to a telecommunications network.

Second, the City argued that the fee was wholly severable from the connection and thereby could still be assessed on all new construction. The Court found the court of common pleas correctly refused to sever the fee requirement based upon the Ohio Supreme Court's three part test for severing partially unconstitutional laws: (i) whether provisions are capable of separation, (ii) the connection with the general scope of the whole, and (iii) whether insertion of words is necessary to separate the constitutional from the unconstitutional portion. The Court affirmed the court of common pleas holding that the fee was only partially severable – it could be assessed only as to those new units requesting a System connection.

The Court affirmed the denial of 1983 relief because the United States Supreme Court created a special rule for Section 1983 claims requiring exhaustion of state law remedies and in this case, the Homebuilders could have sought mandamus. Because the Homebuilders were not entitled to Section 1983 relief, the Court held they were not entitled to attorneys' fees.

As to the issue of taxpayer standing, the court explained that to have taxpayer standing, a party's aim must be to enforce a public right and not where the goal was the taxpayer's own benefit. In this case, the Court found that the Homebuilder's goal was sufficiently private and therefore upheld the finding of the court of common pleas. Judgment of the court of common pleas affirmed.

Comment 1: The City couldn't just add the cost of the connection to other fees because it was related to a service that could only be provided through a wire that the City had no right to connect. It couldn't claim it was a tax, presumably, because of uniformity of taxation requirements.

Comment 2: So, installing the wires is a taking. Then why doesn't the City just compensate the homebuilders and go ahead with its installations? And why was the appropriate relief an injunction, which the court granted? As to the former, the City probably had the option to do this, but elected to forego the opportunity, since it couldn't collect the fee from non-consenting homes. But would the required compensation for those itty bitty wires really amount to much?

Comment 3: Stepping back from this particular dispute – what exactly is going on here? Why is a city entering into this highly competitive area of telecommunication access? Certainly not because private industry is not providing the equivalent service. (Time Warner Cable attempted to intervene in the case but was denied standing.) And certainly not because there is a critical public need. The City wasn't giving away its service, it was selling the service. Why should a municipal agency be able to flex its considerable tax free power to compete to provide service that it being readily provided through private sources? There's a story here.

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, in the view of the court, were independent of the limited warranty, the court held that the plaintiffs could assert a breach of contract claim against the developer.

Comment: Of course, in many states, contractor interests have been able to influence the legislature to adopt rather detailed statutes relating to the preclusion of implied warranties by express warranties, and undoubtedly some of these statute bar a variety of related claims, such as breach of contract.

Nevertheless, in many jurisdictions, the theories espoused here will provide a useful "end run" for unhappy customers.

DEEDS; DESCRIPTIONS: Reference to subdivision lot by lot number "per the recorded plat thereof" adequately incorporates recorded amendments to the plat that revise the boundaries of the lot in question. ***Goad v. Ulrich, 13 S.W. 3d 738 (Mo. App. 2007)***

DEEDS; VALIDITY; MISTAKE: Although an owner of land may be competent to sign a deed, the owner's diminished capacity may be taken into account in determining whether the owner made a unilateral mistake in understanding the compensation to be paid. Further, in any event, a court of equity will set aside the deed for inadequate compensation. ***Landers v. Sgouros, 2007 Westlaw 1575879 (Mo. App. 6/7/07)***, discussed further under the heading: "Waste, Life Estate; Timber."

The case is somewhat involved, but provides an interesting insight into judicial treatment of a transaction that equity suggested should be undone, where concerns about consistency in legal treatment of land transactions suggested that the transaction should be undone on the narrowest possible grounds.

Landers, an 85 year old widow, owned an interest in certain property including some pasture and timber land – a total of 370 acres. She leased the pasture land for $2400 per year.

Through the transactions described here, Landers sold her entire interest in this property to Sgouros for $500. Although Sgouros was a stranger to Landers, another party, Johnson, a 20 year neighbor and alleged friend of Landers intermediated in the transaction and even drove Landers to the closing. There was no evidence at trial that Johnson received anything from Sgouros for his assistance, and Johnson maintained that he was just helping his neighbor and new acquaintance Sgouros get together on a deal.

The evidence showed that Landers first contacted Johnson about possibly selling her interest in the property to him for a price of $150,000. He responded that he was not interested in buying, but he introduced her to Sgouros, who was interested.

Sgouros produced a contract for the sale of the land for $150,000 and Johnson accompanied the parties to a bank, where Landers executed the contract. Landers believed that she would be paid at that time, but she was not. The attorney prepared contract provided for a title examination and a separate closing thereafter. Upon examination of title, Sgouros determined that it was probable that Landers owned only a life estate in the property and arguably a one half undivided fee interest in about a third of it. Sgouros then instructed his attorney to draw up an amendment to the contract providing that he would pay $500 for Lander’s interest. Johnson put the amendment in Lander’s mailbox and she signed it. Later, Johnson drove Landers to a closing, at which Landers executed a deed and received a check for $500.

Landers, although 85, was not incompetent, and knew that she was selling her land. She understood the uncertainty of title, and the reasons for it (she and her late husband had transferred an interest to some relatives and later sought to get it back.) She testified that she believed that she was to receive a payment of $44,000 for her interests, in light of the title problem. She also testified that she received $1000 at the closing, but it appears that she did not. Further, no document that provided for payment of $44,000, or for an installment payment arrangement at all.

Shortly thereafter, after terminating the pasture agreement, Sgouros sold the hay on the land for $600 and sold the timber on a portion of the land, receiving an initial payment of $3950, under a contract that would ultimately pay him around $30,000.

Later, when Landers sought to challenge the deed, the trial court set it aside based on her demonstrated lack of competency at the hearings and the undue influence of Johnson, who had, the court concluded a “quasi-confidential” relationship with Landers as her neighbor and friend.

The appeals court, however, concluded that there was inadequate evidence of incompetence *at the time of the transaction*. Landers had not been declared incompetent and the court’s observation of Landers occurred almost a year after the transactions in question. There was evidence that she felt that she had been swindled and that she believed the land was worth more than she received, but the appeals court concluded that, contrary to supporting a claim of incompetency, this evidence in fact showed that she was aware of what she was doing.

At to the issue of undue influence, the court admitted that diminished capacity is relevant in determining whether there has been undue influence, but that there still was no showing here that such influence existed:

“[W]hile there was evidence from which the trial court could possibly conclude there was, as the trial court terms it, a “quasi-confidential relationship” between Mr. Johnson and Mrs. Landers, it is clear that a “confidential relationship . . . alone is not enough to raise a presumption of undue influence . . . .” [citation omitted]. Further, there is even less evidence creating an inference that there was a confidential relationship, a quasi-confidential relationship, or a fiduciary relationship between Mr. Sgouros and Mrs. Landers. Based on the foregoing we are persuaded, under the applicable standard of review, that “[t]here was no evidence demonstrating the actual exercise of undue influence, only that from which a suspicion of its exercise, or the opportunity to do so, could have been said to exist . . . .”

So far, it looked like the “wrong side” would win. Right? But the appeals court was up to the challenge. The editor can hardly state the steps of the analysis more succinctly than the appeals court (omitting the citations.)

"Although "inadequacy of consideration is insufficient to warrant relief in the absence of other inequitable incidents, when a person is induced to part with an item of value for little or no consideration, 'equity will seize upon the slightest circumstance of fraud, duress, or mistake for the purpose of administering justice in the particular case.'". . . In our analysis of the facts we are guided by principles of equity, real estate and contract law.

'[W]here a grantor has been induced to execute a deed conveying something of value for little or no consideration, equity will grant cancellation if the conveyance was the product of fraud, duress or mistake.' We also note that "equity entertains jurisdiction to set aside a land conveyance to aid a party otherwise unable to obtain relief.' . . . "Parol evidence is admissible to show the actual consideration for the deed.' '[C]ontractual provisions as to consideration to be paid by the purchaser are ordinarily not merged in the deed, and accordingly, evidence is admissible to show what consideration is to be paid although a deed has been accepted . . . .' Tested by these principles, it is our view that Mrs. Landers was confused and mistaken as to the consideration she was to receive for the conveyances pursuant to the Amendment to the Contract.

'A unilateral mistake occurs when only one party has an erroneous belief as to the facts.' . . . We recognize, of course, that [i]n this situation courts show a lack of sympathy for a claim that one party did not understand the consequences of an act and, in general, courts are very reluctant to allow one party or his representative to avoid a document or agreement for a mistake that was not shared by the other. . . .

'Although traditionally there has been reluctance to allow a unilateral mistake to avoid an agreement, this strict view has, in limited instances been softened, and a limited right of avoidance has been recognized." . . . 'It has been stated that there may be relief by way of rescission for such a mistake when the other party knows of the mistake or it is so obvious that it should have been known.' 'Recently, there has been a tendency to permit avoidance for a unilateral mistake when enforcement would be unconscionable and relief would impose no substantial hardship on the other party.' . . . .Indeed, "[t]he Restatement [2nd of Contracts – Sec. 153] recognizes that relief may be given for a unilateral mistake when (a) the effect of the mistake is such that enforcement would be 'unconscionable' or (b) the other party had reason to know of the mistake.' . . . . 'While the distinction between a mistake of fact and a mistake of law is often blurred, it is generally recognized that there can be no relief for a mistake of 'law.'

Here, while the evidence may support the proposition that Mrs. Landers made a mistake in law, the evidence also supports the proposition that she made a mistake in fact when she signed the Amendment which set out that she was to convey her interest in the Farm for $500.00. We agree with the trial court's conclusion that she believed the $500.00 she received at closing was a down payment on the total purchase price of $44,000.00."

Comment 1: Yes, yes, it is somewhat difficult to argue that a competent person would sign a contract to sell for $500 and believe that she was agreeing to sell for $44,000, especially when the figure $44,000 did not appear anywhere in any agreement. But, as indicated, there was abundant evidence of injustice. The woman sold her interest in the farm for $500 even though she was receiving $2400 per year for the pasture rights alone. (The pasture payment belong entirely to her as a life tenant). The fact of her age, her obvious state of confusion less than a year later, and the injustice of the price led the court to conclude "enough's enough."

Further, it was difficult to argue that the buyer wasn't aware of the inequities here, since the buyer quickly capitalized on his good deal by recovering the sale price in the sale of the existing hay on the property and attempted to sell the timber rights for a good deal more. In addition, the buyer thought that he was buying not only the timber rights but probably an undivided one half interest in 120 acres as well. The buyer arranged with Landers to sign two deeds so that he could maintain his case on the fee interest.

Comment 2: Courts have to have discretion to make things right in individual transactions when they "smell a rat." But it is important for them to select very narrow, fact based, grounds, that will not create uncertainty in the general run of transactions, and further to insure that parties relying in good faith on apparently appropriate deals are not undone when special facts exist that are unknown to them. Here, the defendants should have known that their deal was suspect. And the egregious difference between price and value, the special circumstances of an 85 year old widow of weak competency, even though she was not wholly incompetent, and the "personal escort" provided by her arguably disinterested neighbor all combined to create special circumstances that differentiate this case from regular transactions, and the well being of the law is secure.

EASEMENTS; SCOPE; PRESCRIPTION: Storm water drainage can give rise to a prescriptive easement, but such an easement is limited in both location and scope to that occurring during the period over which the easement is acquired,***Trenz v. Town of Norwell, 861 N.E.2d 777 (Mass. App. Ct. 2007)***, discussed under the heading: "Nuisance; Storm Water Runoff."

EMINENT DOMAIN; INVERSE CONDEMNATION; AIRPORT NOISE: Noise from aircraft flying within navigable airspace did not constitute an uncompensated taking. ***Biddle v. BAA Indianapolis, LLC, 860 N.E.2d 570 (Ind. 2007)***.

This case concerns plane traffic in airspace over the homes of Biddle and other plaintiffs ("Homeowners"), as well as prior settlements made by BAA Indianapolis ("BAA"). Homeowners live in Hawthorne Ridge, a subdivision located three miles from Indianapolis International Airport. BAA operates the Airport under a contract with the Indianapolis Airport Authority ("IAA"), the municipal corporation that owns the airport.

Landing aircraft fly 1,300–1,500 feet above the Homeowners' homes, and departing aircraft fly 2,000–4,800 feet above the homes. Congress has established 500 feet as the lowest level of navigable airspace. Flights into the Airport subject homes in Hawthorne Ridge to noise. The IAA participates in sales assistance, sound insulation, and guaranteed purchase programs ("land use programs") to mitigate harm to nearby residents, such as those in Hawthorne Ridge.

In 1997-98, IAA and BAA representatives made statements at public meetings, at which none of the Homeowners was present, that the Airport would "treat all neighbors alike," and would not "break up a neighborhood," regarding the three land use programs. In 1999, forty other residents of Hawthorne Ridge ("Backs") filed suit against the IAA and BAA. The parties reached settlement that included a $16,000 payment to each landowner and a guarantee of market price upon sale of their homes, in exchange for an "avigation" easement for aircraft to fly in and out of the Airport.

Homeowners filed suit against the IAA and BAA in 2001. The trial court ruled against Homeowners' claims of inverse condemnation, nuisance, and promissory estoppel at the summary judgment stage. The Court of Appeals reversed and remanded, but the Supreme Court of Indiana granted transfer.

Citing *Aaron v. United States*, 160 Ct.Cl. 295 (1963), the court presumed there was no taking because the airplanes in question were in navigable airspace (above the 500 foot floor). The court also held that the Homeowners did not meet the exception to the *Aaron* rule articulated in *Branning v. United States*, 228 Ct.Cl. 240 (1981), because Homeowners' residential use of their property was not practically destroyed or substantially impaired by aircraft noise.

Homeowners also claimed that the IAA and BAA were estopped from declining to offer them the same settlement as the Backs plaintiffs. The court held that estoppel is generally not applicable against government entities for the actions of public officials, that the public statements in question made by officials were more akin to statements of policy than promises, and that the statements, even if promises, referred to the land use programs and not prospective litigation settlement agreements.

Finally, regarding the inverse condemnation claim, the court found that the Fakes, one of the Homeowners, received formal notice of damage to value of their property upon its purchase. The Fakes had purchased their home at a reduced price specifically because of aircraft noise, knew this at the time of purchase, and therefore could not have seen a diminishment of investment- backed expectations. Accordingly, the court ruled in favor of the defendants, IAA and BAA, on all three claims.

EMINENT DOMAIN; **VALUATION:** . Past owner could be competent to give valuation testimony in eminent domain proceeding under the "owner-opinion" rule, where owner has maintained involvement with the property. ***Proctor v. Vance, 860 N.E.2d 1099 (Ohio Misc. 2006)***. Gordon Proctor, Director of Ohio Department of Transportation ("Plaintiff") commenced a condemnation action on the property of Eva Vance ("Defendant") for the expansion of State Route 28. Plaintiff filed a motion *in limine* seeking an order that Defendant could not elicit testimony from Charles Vance, Defendant's husband and a former owner of the property. Charles Vance conveyed the property to his wife for estate-planning purposes, but continued to be involved with its purchase, development, and lease since the inter-spousal conveyance. The "owner-opinion rule" is an exception to Evid.R. 701 that classifies an owner of real property as competent, without qualification as an expert, to testify about fair market value of the property. The court held that the benefit of the owner-opinion rule should not be denied to a person whose interest is tantamount to that of an owner. For a witness' interest to be tantamount, the witness must show: 1) familiarity with the property itself; and 2) current sufficient knowledge of the value of the property. These requirements can be met by demonstrating firsthand knowledge of characteristics of the property, actual or potential uses for the property, the condition of the property, or other meaningful experience in dealing with the property. Assuming the truthfulness of assertions in Defendant's memorandum regarding Charles Vance's familiarity and sufficient knowledge of the property, the court held that his testimony as to value of the property should be admitted. Plaintiff's motion denied.

ENVIRONMENTAL LAW; CONTAMINATION; DAMAGES: The correct measure of damages for environmental injury to real property depends on whether the injury is permanent or temporary, which is an issue of fact for the jury. If the injury is temporary, the measure of damages is the cost of repair or remediation. If the injury is permanent, the measure of damages is the diminution in value of the entire property, not just the part that is injured. ***McNeill v. Burlington Res. Oil & Gas Co., 2007-NMCA-024, 141 N.M. 212, 153 P.3d 46 (12/4/06; cert. granted, No. 30,162, 2/9/07).***

Plaintiffs were the owners of the surface rights of the McNeill Ranch. Defendant was the former oil, gas, and mineral lessee under a portion of Plaintiff's property. Defendant's predecessor-in- interest owned and operated an oil well on a tract of land on the McNeill Ranch. The oil well ceased production in 1986, and in 1992 Defendant closed the pit. Around 1996, Plaintiff William McNeill learned of the pit and possible contamination, so he contacted Defendant and asked for the contaminated materials to be removed. Defendant did not remove the contaminated materials.

On June 1, 1999, Plaintiffs filed suit, and on January 13, 2000, they filed an amended complaint alleging negligence, trespass, and private nuisance for contamination of their property resulting from Defendant's operation of an oil well. Defendant raised numerous affirmative defenses, including but not limited to, statute of limitations, estoppel, waiver, and release. On appeal, the New Mexico Court of Appeals held that Defendant's defenses were without merit.

In analyzing Plaintiff's arguments pertaining to jury instructions and damages, the Court of Appeals concluded that the correct measure of damages for injury to real property depends on whether the injury is permanent or temporary. The determination of whether an injury to real property is permanent or temporary is a question of fact to be decided by the jury. While this distinction tends to be problematic, "[t]emporary damages are generally defined as damages that can be remedied, removed, or abated within a reasonable period and at a reasonable expense." *Id.* ¶ 27 (*citing Morsey v. Chevron, USA, Inc.*, 94 F.3d 1470, 1476 (10th Cir. 1996)). "In contrast, permanent damages are defined as those damages caused by an injury that is fixed and where the property will always remain subject to that injury." *Id.* ¶ 28 (*citing Morsey v. Chevron, USA, Inc.*, 94 F.3d 1470, 1476 (10th Cir. 1996)). "If the injury is permanent, the correct measure of damages is the diminution in fair market value of the ***entire*** property," not just the portion of land that is physically injured. *Id.* ¶ 37 (emphasis added). "If the injury is temporary, then the correct measure of damages is the cost of repair or remediation." *Id.* "If the cost of repair or remediation is greater than the diminution in fair market value, then the latter is the correct measure of damages." *Id.* Even if the jury finds that the injury is permanent, and thus the correct measure of damages would be diminution in fair market value, evidence regarding cost of repair or remediation should be allowed.

The Court also discussed stigma damages and noted that the decrease in fair market value of the property necessarily takes into account any stigma associated with the property as a result of the injury.

HOMESTEADS; TRANSFER TO TRUST; HOME-STEAD EXEMPTION; TITLE INSURANCE: A Chapter 7 bankruptcy debtor may claim the homestead exemption where the real property was transferred to a revocable trust prior to the bankruptcy and the bankruptcy debtor was both the settlor and a beneficiary of the trust. ***Redmond v. Kester, 2007 WL 1649931 (June 8, 2007).***

This case was certified to the Supreme Court of Kansas from the Tenth Circuit Court of Appeals regarding the application of the Kansas homestead exemption in a bankruptcy proceeding. Donald and Charlotte Kester purchased a home by warranty deed in 1994, and in 1996 they transferred it, via quitclaim deed, to the Charlotte Kester Trust, a revocable trust with Charlotte Kester as the trustee. Both of the Kesters were named as beneficiaries of the Trust. In 2002, the Kesters filed a Chapter 7 bankruptcy proceeding, claiming the house as exempt under Kansas law. The bankruptcy trustee objected to the claimed exemption, asserting that the debtors were not entitled to the exemption because the real estate was owned by a trust rather than the debtors, and therefore they did not have an interest in the real estate after they voluntarily executed a quit claim deed transferring their interest in the real estate to the trust.

The Kansas Supreme Court examined the codified Kansas homestead exemption, which originated in the Kansas Constitution, and the cases interpreting the exemption, and concluded that "courts must liberally construe the constitutional provision without restricting its application (citation omitted)." *Id.* at *3. The court also concluded that a beneficiary has an equitable interest in real estate owned by the trust and that an equitable interest is sufficient to claim the homestead exemption; i.e., as long as the claimant occupies the real estate, the trust was entitled to claim the homestead exemption under Kansas law. The court bolstered its holding by quoting from another Kansas statute, which provides, in relevant part, that "The transfer by warranty deed of real property into an inter vivos trust shall not affect the coverage of any title insurance if the settlor of such trust is and remains a beneficiary of such trust during the settlor's lifetime." K.S.A. 58-a-1107. This statute also provides that upon the transfer taking effect, the trustee shall be deemed to be the insured under the original title policy, and that the transfer shall not affect any exemption or homestead rights.

The bankruptcy trustee argued that this statute did not apply to the facts of this case because the statute was not retroactive and the debtors did not transfer the property to the trust via a warranty deed. But the court found that the statute did in fact apply retroactively, and that regardless of the requirement of a warranty deed in K.S.A. 58-a-1107, *supra*, the precedent established since the inception of the Kansas Constitution established that the term "owner" as used in K.S.A. 60-2301 applied to the holder of any interest in real estate, regardless of whether the interest was in fee simple. The court stated that "Defining the term 'owner' in K.S.A. 60-2301 broadly to include occupants of real estate who hold any type of interest, including an equitable interest, is consistent with the public policy of protecting Kansas citizens from the hardships associated with losing the family home." Id. at *6. The court found that the definitions of the term "owner" in existing case decisions "reflect the liberal protection intended by the framers of our state constitution when they crafted the homestead provision." Id. at *4.

Reporter's Comment 1: Kansas has a statute, K.S.A. 58-a-1107, which specifically provides that title insurance coverage continues when property is transferred by warranty deed into an *inter vivos* trust. Normally, however, where there is not such a statute (I am not aware of any other state that has such a statute), this is not the case. The 1992 ALTA Owner's title policy definition of "insured," as set forth in Paragraph 1(a) of the title policy Conditions and Stipulations, includes "those who succeed to the interest of such insured by operation of law as distinguished from purchase." See *Covalt v. First American Title Insurance Co.*, 105 F.3d 669, 1997 WL 4273 (10th Cir. Jan. 7, 1997) (unpublished disposition) (ruling that transfer of real property, by quitclaim deed, from individual to trust in which individual retained an interest, prevented trust from claiming any rights under the title insurance policy originally issued to individual); *Butera v. Attorneys' Title Guaranty Fund, Inc.*, 321 Ill. App. 3d 601, 607, 747 N.E.2d 949, 954 (2001) (holding that a deed from a trust to corporation, whose shareholders were the sole beneficiaries of the trust, was a transfer by purchase and not a transfer by operation of law that would provide continuing coverage under the owner's title policy originally issued to the trust); *Austin v. City of Alexandria*, 265 Va. 89, 95-96 (2003) (holding that deed to trustee effects change in ownership of property even if grantor, trustee, and beneficiary are same person and beneficiary has complete power to revoke trust).

Standard title insurance policies define an "insured claimant" as an "insured" claiming loss or damage. See ALTA Owner's Policy, Conditions & Stipulations, par.

1(b) (Oct. 17 1992). Therefore, as noted in the cases described above, the title insurer will likely reject a claim by a party who is neither the insured named on Schedule A nor a "successor" thereof by "operation of law."

Reporter's Comment 2: Under the new 2006 ALTA Owner's and Loan 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 estate-planning purposes.

Editor's Comment: Note that Kansas is one of those states that has a "no value limitation" homestead exemption. Thus, parties facing potential financial difficulties typically dive into expensive residential properties (if they can get it done soon enough) and preserve assets enough to compel creditors to make generous settlements.

The Reporter for this case was Jack Murray of the Chicago office of First American Title Insurance Company.

LANDOWNER LIABILITY; ELEVATORS: Maryland upholds old majority rule that owners of building containing elevators are treated as common carriers with high standard of care to prevent injuries to riders, even in modern area of safer, self-service elevators. ***The Johns Hopkins Hospital v. Corriea, 921 A. 2d 837 (Md. App. 2007)***

Plaintiff claimed serious aggravation of an existing back injury when a slow, low level elevator lurched. There was evidence that the elevator had some parts that had worn, and that there had been similar incidents involving this elevator in the past. But Johns Hopkins had contracted with a professional elevator operating company to maintain the elevator systems.

The court determined that it would adhere to the established law in Maryland and the majority of other U.S. jurisdictions:

> [O]ne who "is engaged in the undertaking of running an elevator as a means of personal transportation" is required to use the "highest degree of care and diligence practicable under the circumstances," which is the same standard that common carriers are required to meet."

The court noted that this standard applies to the owner of the building in which the elevator operates, and does not apply, interestingly enough, to the operating company employed to operate and maintain the elevator.

Defendant Hospital argued that the rule in Maryland dated back to 1937, and there was some small authority to suggest that Maryland cases since them did not follow it. Hospital noted that when the rule was developed elevators were much newer technology and, moreover, were generally operated by employees of the building owner who "drove" them. Thus the rationale for treating them as a common carrier was more evident. In modern times, however, the Hospital argued, the proper standard ought to be the duty of reasonable care that an owner owes to building invitees generally in Maryland.

The court disagreed.

> "The foundation of the rule for the protection of a passenger is in the undertaking of the common carrier which is to carry safely; but another reason for it is, that when the passenger commits himself to the carrier he does so in ignorance of the machinery and appliances (as well as their defects) used in connection with the means of transportation, and becomes a passive and helpless creature in the hands of the transportation company and its agents. For the same reason, this rule should be extended to those who operate elevators for carrying passengers from one story of a building to another. When they undertake to carry they undertake to carry safely.

> If it is not their express agreement to do so, it is surely an implied one, and the condition of a passenger caged in a suspended car, is one not only of utter ignorance of what has been done or ought to be done for his safety, but of absolute passiveness and pitiable helplessness when confronted with danger against which human knowledge, skill and foresight ought to have guarded; and the rule has been so extended."

Because elevator passengers today remain "passive and helpless creatures," albeit now independently able to push the buttons to make the car move, the court concluded that the same rationale ought to apply. It noted that 21 other states follow this approach, while a much smaller number use the ordinary care standard.

Hospital also argued that the application of the duty to it was inappropriate because, like most building owners, it maintained an independent company to service its elevators. The court noted that here the allegations of negligence included a failure of the building owner to report incidents suggesting elevator problems to its operating company. In any event, however, the court concluded that it is the owner of the elevator that invites riders to use it and is most likely to become aware of operational problems. Therefore, it is appropriate that the high duty be imposed upon the owner, and such duty is non delegable.

Comment 1: Note that the court, citing authority elsewhere, does not extend the rule to escalator operators.

Comment 2: Comment 1: Note that the court, citing authority elsewhere, suggests that the same rules ought to apply to escalators.

> "Nine states hold that the duty owed by an operator or owner of an escalator is merely to exercise ordinary care. Five states, however, hold that under the common law the owner/operator of an escalator owes the passenger the highest degree of care. Two states, California and Georgia, have enacted statutes imposing upon the owner/operator of an escalator the duty to use the highest degree of care.

LIS PENDENS;* CONRUCTIVE NOTICE:** Filing of *lis pendens* with county recorder does not impart constructive notice until indexed, even if delivered to the recorder a week earlier. ***Dyer v. Martinez 147 CA4th 1240, 54 CR3d 907 (2007), discussed under the Heading: "Recording Acts; *Lis Pendens.*"

MARITAL PROPERTY; TENANCY BY ENTIRETIES; MORTGAGES: Where deed of trust states, in its granting clause, that it is given by a named individual, a married man, but the property at the time is owned in tenancy by the entireties, when the individual dies and his spouse's survivorship right takes effect, the deed of trust disappears, *even though the surviving spouse in fact executed the mortgage and benefitted from the expenditure of the proceeds.* ***Ethridge v. TierOne Bank, 2007 Westlaw 1816853 (Mo. 6/26/07)***

You can get an idea as to how this opinion will go from the opening lines:

"When David Ethridge refinanced the home that he and his wife, Mary, held as tenants by the entirety, the lender prepared loan documents that slighted the wife. As the wife later said, her husband was "head of the household." That legally quaint assumption appears embodied in the lender-drafted refinancing papers that list David Ethridge, a married man, as the sole owner and the sole borrower. The law, as set forth in precedent cases dating to 1887, is harsh and unforgiving of such slights.

TierOne Bank, successor to the refinancing lender, seeks to impose the obligations of borrower on Mary Ethridge now that her husband is dead. To allow Mary Ethridge to retain the home free of the refinancing lien, the bank says, is unjust. The law, however, is unforgiving of the injustice of slighting the wife's interests at the time of refinancing – that injustice produces an enrichment of the wife who has no obligation to pay her late husband's loan. Equitable doctrines will not help. The bank loses."

It appears that the bulk of the money borrowed in this financing went to retire an earlier mortgage loan on which, presumably, both spouses were liable. The balance was used to pay for improvements to the premises that the wife now owns outright (her husband was killed in a traffic accident.)

Apparently David Ethridge, who, as the court admits, handled the couple's financial affairs with Mary's acquiescence and consent, negotiated this loan and likely executed the application by himself, showing his own assets and income, other than the home. The closer at the loan closing therefore listed the "borrower" in the blank provided as David alone. Other parts of the standard form mortgage indicated that the borrower warranted that he owned the property given as security. Mary, however, appeared at the closing and executed the deed of trust under David's signature and also executed a closing statement.

There can be no doubt that Mary intended by these acts to authorize that the tenancy by entireties property would stand as security. Unlike a joint tenancy in Missouri, a tenant by the entireties has no separate interest in the entireties property. A deed of trust cannot attach to a partial interest or an expectancy. If the deed of trust is not executed by both parties, giving the entire interest as security, nothing would be given. Consequently, Mary's execution of the deed of trust had no meaning other than the commit the property to the deed of trust. And, of course, she acquiesced in the security arrangement and the distribution of the proceeds.

Nevertheless, the court held that Nineteenth Century Missouri authority was to the effect that a conveyancing instrument that does not properly recite the owner's granting intent in the granting clause does not convey that interest, even if the owner executes the instrument: "The party in whom the title is vested, [sic] must use appropriate words to convey the estate. Signing, sealing, and acknowledging a deed by the wife in which her husband is the only grantor, [sic] will not convey her estate."

But the lender argued that the deed of trust should be reformed because it was evident that Mary intended that it convey her interest. The court rejected this argument, holding that reformation doctrine does not support that outcome here:

". . . Reformation presupposes a valid prior agreement evidencing a meeting of the minds," which is simply not present here. . . . [T]here is no evidence that there was a scrivener's error. The evidence reflects that David Ethridge and the lender had a prior agreement that was, in fact, accurately reflected in the deed of trust. David Ethridge intended to grant the lender a lien on the property and the lender intended to hold the lien.

. . . [T]here was no mistake as to the parties' intent. There is no clear, cogent, and convincing evidence that it was Mary Ethridge's intent to grant a lien to the lender or that there was a mistake in drafting the deed of trust. The doctrine of reformation cannot be applied."

There was a strong dissent from two of the seven members of the court.

Comment 1: This opinion is ridiculous. It goes beyond being simply a careful reading of the conveyancing laws. The tenancy by the entirety in Missouri is indivisible. The husband had no interest to give as security except the entirety interest – belonging to both him and his wife. If she hadn't signed, no loan would have been possible. How could the court conclude that the parties apparently intended a null act?

The court makes the absurd claim that the wife was somehow being treated "unjustly" when only her husband signed the note, with both of them signing the deed of trust. In fact, this is not an uncommon event. One party commonly might assume personal responsibility for a debt but other parties may agree that property that they own jointly with the debtor will stand as security for that debt. In fact, if the bank had insisted that, even though the husband qualified for the loan on his own merits, the wife would have to sign the note, this would have violated the Federal Equal Credit Opportunity Act. Here, the wife not only was not the victim of injustice, but got a significant economic benefit. The money was actually used to refinance a debt to which the wife was a signatory and to carry out improvements to the home that the wife came to own outright when her husband died.

Equally absurd is the court's proposition that the wife had no intent to give her home as security for the loan. She showed up at the closing office and executed a closing statement and a deed of trust. It is wholly illogical to argue that she had no notion that she was agreeing that the home should stand as security for the loan. Although the husband had negotiated to that point with the lender, the court indicates that he had done so with the authority of the wife – that he was responsible for all the couples financial affairs.

The case for reformation was easy. What the scrivener got wrong was the identification of a single party as the "borrower." The "borrower," for purposes of the deed of trust, consisted of the entireties estate, and that should have been set forth at the beginning of the deed of trust. There certainly was a form for this, and the scrivener just used the wrong form, and thus there was a common technical mess up.

Comment 2: It is true that lenders frequently botch up the paperwork for borrowings by an individual spouse. I typically execute deeds of trust securing my wife's borrowings in order to release my marital interest in her separate property securing the loan – her farm property. The signature lines on these documents always show me as the 'borrower," and I always cross that out and put "executed for purposes of waiver of marital interest." I don't wish to be liable on the title warranties or other covenants in the mortgage when it's not my property or my loan. Of course, if the property was entireties property, I wouldn't object to be liable on those warranties, and therefore should be listed as "trustor." Still, if only one spouse signs the note, the deed of trust ought not to list both as the "borrower" on the deed of trust. It's likely to cause trouble down the road.

But how much can you expect of low paid paper pushers in these closing offices? The court's decision here ignores the fact that the wife attended the closing, got the money, and had all along acquiesced in her husband's management. It's an unjust result, and one that might occasion some difficult new closing practices in Missouri, and perhaps in other tenancy by entireties states.

MORTGAGES; NOTES; NONRECOURSE; ENFORCEABILITY OF CARVEOUTS: First reported decision in which a court has enforced recourse of "bad boy" carveouts in a nonrecourse securitized loan. ***Blue Hills Office Park, LLC v. J.P. Morgan Chase Bank, 477 F. Supp.2d 366 (D. Mass. 2007)***

The borrower settled a dispute with a neighboring landowner concerning the neighbor's attempt to get zoning that would permit it to erect a parking garage on its property. The borrower withdrew its appeal of a zoning ruling in return for a cash payment of $2 million. It pocketed the money and provided no notice the lender. The court ruled that the settlement was part of the "mortgaged property," which, as described in the loan documents, included "[a]wards or payments . . . with respect to the Premises . . . for any . . . injury to or decrease in value of the Premises."

The nonrecourse provision in the mortgage (which obviously was carefully negotiated) specifically provided that if the borrower diverted funds from the mortgaged property that belonged to the lender, the borrower's and guarantors' liability would become recourse for the entire loan balance of the loan (certain other borrower acts and defaults, such as fraud, intentional physical waste, or removal and disposal of mortgaged property after default, would result only in limited liability of the mortgagor and guarantors for actual damages).

The court held that when the borrower settled a zoning appeal against the adjoining landowner (in this case for $2 million) and failed to disclose the settlement to the lender or seek its consent (as required by the mortgage loan documents) and diverted the funds to itself, the borrower (and the guarantors) lost their nonrecourse protection and became liable for the full amount of the deficiency and other costs (upwards of $20 million), and not simply the restitution amount of $2 million. (The high bidder at the lender's foreclosure sale, instituted after the borrower defaulted on its loan payments, was a single-purpose entity created by the lender, which later sold the property to a third party.)

The court castigated the attorneys for the borrower and the guarantors. Apparently these attorneys assumed that since litigation in this area is so rare, they could assume a very aggressive litigation posture and the matter would be worked out later to their satisfaction. But the moral of the *Blue Hills* case is that carveouts to nonrecourse loans mean what they say and will be strictly enforced (even if the borrower and guarantors rely on advice to the contrary from their counsel)! (See John C. Murray, "Carveouts to Nonrecourse Loans: They Mean What They Say!" http://www.firstam.com/listReference.cfm?id=5574.)

After the court's judgment, the guarantors fired their attorneys and put them on notice of a malpractice claim. The borrowers and guarantors subsequently appealed from the judgment, but the appeal was dismissed and $17.25 million (98.5% of the judgment) was paid to the lender to settle the case. (Blue Hills Settlement and Release Agreement.) As Judge Young so succinctly stated during the trial, "don't mess around with the collateral. . . . "[I]f you mess around with the collateral, that's when you'll be liable for the entire amount of the deficiency." 10/13/06 Blue Hills Case Trial Transcript at 47.

The court also found a second violation of the nonrecourse carveouts – the borrower had violated single-member and single-purpose-entity requirements in the loan documents by commingling the $2 million settlement payment with monies of its member and by failing to maintain a participating independent director. Although the borrower had named as the "independent director" an individual who once worked as a paralegal or secretary at the borrower's law firm, the court stated that "it is clear that she did not participate in the management of Blue Hills in that capacity," *Id.* at 383, and that she "was not involved in the discussions concerning the $2,000,000 settlement payment." *Id.* Therefore, the court held, the borrower had violated a specific mortgage covenant because it had failed to "cause there to be" an independent director and had failed to maintain its status as a single-purpose entity. *See In re Kingston Square Associates*, 214 B.R. 713, 721 (Bankr. S.D.N.Y. 1997) (finding for plaintiffs partially on basis that "[the "independent director"] seems not to have taken any interest at all in the properties. He testified that as a director he never reviewed any documents regarding any of the Debtors including rent rolls, judgments, or state court decisions").

Reporter's Comment 1: Since the mid-1980's, lenders have been qualifying and restricting nonrecourse provisions in commercial real-estate loans by making exceptions for certain "bad acts" by borrowers. In recent years, many lenders have expanded the scope of such "carveouts" to include risks of exposure to the property's economic deterioration or neglect. Some nonrecourse provisions provide that the borrower is liable for the specific damages resulting from the violation or breach of a carveout, while others state that the entire loan becomes recourse to the borrower if any of (or certain of) the excepted acts occurs. In some cases the exceptions have virtually swallowed the rule; i.e., the clause is drafted so that the borrower has personal liability for virtually all defaults except the failure to pay the principal and interest due on the loan. There has been relatively little case law regarding the validity and enforceability of such carveouts, and these provisions have rarely been challenged by borrowers. However, recent court decisions such as *Blue Hills, supra*, and *Heller Financial, Inc. v. Lee*, Case No. 01 C 6798, 2002 U.S. Dist. LEXIS 15183 (N.D. Ill., August 16, 2002) (where the court rejected a challenge to the enforceability of a specific exception to the nonrecourse provision in the note executed by the borrower) may provide some needed guidance in this area.

Reporter's Comment 2: The court summarily rejected the borrower's bogus lender liability claims (alleging that the special servicer had wrongfully denied its request to access reserve accounts to make the loan payments and real estate tax payments, and that the lender had breached the "implied covenant of good faith and fair dealing" by failing to meet with the borrower in an effort to work out the loan). The court held that the lender was perfectly within its rights in failing to meet with the lender after the occurrence of an acknowledged loan default and was under no obligation to transfer funds from special reserve accounts to make scheduled payments of principal and interest on the loan.

Reporter's Comment 3: As noted above, the court endorsed an expansive definition of "mortgaged property," as broadly defined in the mortgage's granting clauses, to include non-real estate assets only indirectly related to the mortgaged real estate, i.e. a lawsuit brought by the borrower and its settlement proceeds. But might this type of action also be characterized, under somewhat similar circumstances, as a security interest in a tort claim under Article 9 of the Uniform Commercial Code? Could there be a potential conflict? See Prof. Daniel Schecter, Proceeds Resulting from Settlement of Zoning Appeal Are Part of Mortgaged Property and Belong to Mortgage Lender. Blue Hills Office Park LLC vs. J.P. Morgan Chase Bank, 2007 comm. fin. news 26 (April 2, 2007) (Comment):

I wonder whether under a different set of facts, the characterization of the settlement proceeds as "mortgaged property" might create a potential priority conflict with Article 9 of the UCC, which (under some circumstances) permits secured parties to take security interests in commercial tort claims. Suppose, for example, that a borrower's shopping center is injured because a neighboring entity is emitting unpleasant odors thus constituting a nuisance. If the borrower brings a suit against the neighbor on a nuisance theory, that tort recovery might belong to the Article 9 lender with a security interest in the borrower's commercial tort claims. At the same time, the same recovery might be characterizable as part of the "mortgaged property" belonging to the mortgage lender. (Even if there were a potential conflict, the best solution would be a timely intercreditor agreement between the two lenders.)

Reporter's Comment 4: The issue may well be the distinction between the grant of a security interest and the perfection of the security interest in the collateral. The granting clause in a mortgage may be sufficient for attachment as meeting the security interest requirement of §9-203(b)(3)(A) of the UCC. But the filing of a mortgage cannot perfect a security interest in personal property other than fixtures. For example, the granting clause in a mortgage could not define trucks located on the property as "mortgaged property," then try to perfect a security interest in certificated goods through recordation of the mortgage. The correct reasoning undoubtedly is that "mortgaged property" must ultimately be actual real property (or fixtures). A UCC filing clearly would be necessary where a mortgage loan is secured by equipment, personalty or contract rights. Although a mortgage that also constitutes a fixture filing will create and perfect a valid security interest in the fixtures, there is a chance that what the secured party believes are "fixtures" are in fact just equipment. Section 9-102(a)(4) of the UCC (which defines fixtures) should be studied carefully. If the described collateral is not in fact "fixtures," then a fixture filing — or a mortgage that serves as a fixture filing — will not perfect a security interest in the collateral. Comment 6 to UCC §9-503 states, in part:

"In some cases, it may be difficult to determine whether goods are or will become fixtures. Nothing in this Part prohibits the filing of a "precautionary" fixture filing, which would provide protection in the event goods are determined to be fixtures. The fact of filing should not be a factor in the determining whether goods are fixtures."

Therefore, when in doubt it may make sense for the secured party to take the conservative approach and also file a regular UCC financing statement in the "location" of the debtor, with a collateral description of any collateral that may potentially be deemed to be personal property.

Editor's Comment: The editor believes that the lesson here is that "bad boy" clauses *may* mean what they say, and that therefore lawyers counseling borrowers and guarantees should so assume. But the editor is not convinced that the courts have totally abandoned the notion that provisions creating a penalty for default are not enforceable.

Consider, for instance, if the sole violation in this case had been the appointment of the paralegal as the independent director. Assume that, after the lender complained about this appointment (which of course was a callous disregard of the spirit of the independent director requirement), but before any ill consequences had occurred, the borrower agreed to appoint a true independent director. Later, if a default occurs, would the court conclude that the "bad boy" clause operated to destroy the nonrecourse protection? The editor believes that in such cases – harmless or relatively harmless violations or cured violations – even deliberate and callous – the courts may view the loss of nonrecourse protection as a penalty. He's certainly not willing to assume otherwise after just one case.

The Reporter for this case was Jack Murray of the Chicago office of First American Title Insurance Company.

MORTGAGES; PREPAYMENT; PREPAYMENT PENALTY; WAIVER: Lender does not waive right to claim a prepayment penalty for a voluntary prepayment according to the loan documents when it accepts a partial prepayment in connection with a refinancing. ***Great Plains Real Estate Dev. LLC, v. Union Central Life Ins. Co., No. 4:05 – CV – 00220 (U.S.D.Ct. S.D. Iowa 6/4/07)***

Lender and Borrower negotiated a refinancing of this commercial loan at a lower interest rate and better terms. As part of the deal, the borrower paid down the loan by about $360,000. The agreement provided that, except for the negotiated modifications, the terms of the note and mortgage remained the same.

Later, Borrower refinanced again with another lender and objected to the Lender's invoking the prepayment penalty in the loan documents.

The court held that there had been no waiver.

In addition, the court held that Iowa law is that a voluntary prepayment is treated as an optional form of performance for which the parties are free to set a premium charge, which they did here. Further, the court stated, even if the prepayment premium was regarded as a liquidated damages provision, it would be valid. The court cited the *CP Holdings* case for the proposition that a prepayment fee in the form of a yield maintenance clause, using the U.S. Treasury rate as the investment figure to establish the desired yield.

MORTGAGES; SECURITY; TENANCY BY ENTIRETIES: Where deed of trust states, in its granting clause, that it is given by a named individual, a married man, but the property at the time is owned in tenancy by the entireties, when the individual dies and his spouse's survivorship right takes effect, the deed of trust disappears, *even though the surviving spouse in fact executed the mortgage and benefitted from the expenditure of the proceeds.* ***Ethridge v. TierOne Bank, 2007 Westlaw 1816853 (Mo. 6/26/07),*** "Marital Property; Tenancy by Entireties; Mortgages."

MORTGAGES; SUBROGATION; REFINANCING: Another test of the Restatement position, will a refinancing lender with actual knowledge of an intervening lien enjoy subrogation to the refinanced mortgage? ***Bank of America v. Prestance Corp., 2007 W.L. 1631420 (Wn., 6/7/07)***

The question before the Washington Supreme Court was whether a refinancing mortgagor must be precluded from equitable subrogation to a first-priority lien if it has actual or constructive notice of a junior lienholder. The court held that that answer was "no."

The court cited and distinguished *Kim v. Lee*, 145 Wn.2d 79 (2001), where the refinancing mortgagee's title insurer had constructive and actual knowledge of an intervening judgment lien and the court ruled that the title insurer could not avoid liability through equitable subrogation because it had actual knowledge of the lien and refused to disclose it to the insured prior to issuing the title policy)

The facts in this case are somewhat complicated. In 1994, Sakae and Yuko Sugihara ("Borrowers") received a 30-year home loan of $543,000 from Washington Mutual, secured by a deed of trust on their home. In 1999, Bank of America ("B of A") made a loan of $400,000 to Prestance Corporation ("Prestance"), a corporation owned by the borrowers, secured in part by a loan on the borrowers' home. B of A later gave Prestance Corporation an additional line of credit for $1 million, secured by Mr. Sughihara's personal guarantee and an amendment to the deed of trust.

In 2001, the Borrowers approached Wells Fargo Bank West ("WFB West"), for a loan in the amount of $1 million, which was to be secured by a mortgage on the Borrowers' property. The court stated, at par. 4, that:

"One purpose of the loan was to pay off the first-position Washington Mutual [home] loan [in the amount of approximately $500,000]. WFB expected it would then have priority over the other loans for the amount used to pay Washington Mutual. A preliminary title commitment showed the Bank of America loans, secured by the Bank of America deed of trust and its amendment . . . [I]t was WFB West's understanding [when its loan closed] that Bank of America's deed of trust had been (or was being) reconveyed to Wells Fargo Bank ("WFB") and that WFB (a bank related to WFB West) would subordinate its $500,000 loan, putting the WFB West deed of trust in first position."

(In November 2001, Mr. Sugihara received a $500,000 home equity loan from WFB. Part of that loan was used to pay B of A for its original $400,000 loan to Prestance Corporation. Bank of America cashed the check but never reconveyed the deed of trust to WFB.)

Bank of America sued the Borrowers, Prestance, WFB and WFB West, seeking a money judgment and foreclosure of the defaulted B of A loan. The trial court, relying on the Restatement (Third) of Property: Mortgages sec. 7.6 Subrogation (1997) ("Restatement"), ruled that WFB West should be equitably subrogated to the first-priority position of Washington Mutual in the payoff amount of $499,477, which would leave B of A (according to the trial court judge) "in no worse position than it would have been [in] had had [WFB West] never made its . . . loan." Id. at par. 5. The appellate court reversed, holding that under the *Kim v. Lee* decision [see discussion above], "WFB West's actual knowledge of Bank of America's lien barred the application of equitable subrogation." Id. at par 5.

Describing the origins and purpose of the doctrine of equitable subrogation, the Washington Supreme Court stated that, "Borrowed from English courts of equity, equitable subrogation simply seeks to maintain the status quo . . . Equitable subrogation preserves the proper priorities by keeping the first mortgage first and the second mortgage second. Id. at par. 9. The court then adopted the Restatement position, which means subrogation would occur even if the refinancing lender had actual or constructive notice of the intervening lien. Restatement (Third) of Property: Mortgages sec. 7.6 Subrogation 1997. The court also stated that "Despite an initial resistance to equitable subrogation, many courts now apply it liberally" (citations omitted)). Id. at par. 9-10. The court then discussed the three different jurisdictional approaches to equitable subrogation; 1) the

Restatement approach (i.e., actual or constructive knowledge is irrelevant); 2) the "minority" approach that says a plaintiff with either actual or constructive knowledge cannot seek equitable subrogation; and 3) the "majority" approach that says a plaintiff with actual knowledge cannot seek equitable subrogation, while one with constructive notice can.

In its discussion of the majority rule, the court dismissed the argument that applying the Restatement approach would "obstruct the predictability and stability of recording act and the rule "first in time, first in right"; the court stated that "while the recording act provides stability and notice to lenders (both vital elements to any successful real estate lending scheme), we cannot rigidly adhere to its strictures where it works an injustice." Id. at par. 18. The court also dismissed the minority rule, stating that while the rationale for that rule is that a party should not profit from its own negligence by failing to check the public records, "[f]or practical purposes, this rule swallows the doctrine and is widely criticized." Id. at par. 14-15. The court reasoned that if all such persons who confer a benefit on others due to their negligence would be disqualified from equitable relief even where no other party is harmed, "then the law of restitution, which was conceived in order to prevent unjust enrichment, would be of little or no value" (citations omitted)." Id. at par. 15. The court cited with approval a recent law review article by Grant S. Nelson and Dale A. Whitman, Adopting Restatement Mortgage Subrogation Principles: Saving Billions of Dollars for Refinancing Homeowners, 2006 B.Y.U. L. Rev 305, 315-16, in particular the following:

"We have vigorously criticized this approach [the minority rule] and find it impossible to understand in light of the fact that subrogation in this situation harms no one, leaving the intervening lien exactly where it started. In contrast, refusal to grant subrogation gives the intervening lienor an unexpected, unearned, and unwarranted promotion in priority. (footnote omitted)."

The court also justified its decision (allowing WFB West's refinancing mortgage to be equitably subrogated to the first-position Washington Mutual loan even though West knew of the existence of the intervening B of A loan) based on economic considerations, including alleged savings on title insurance premiums and costs. The court stated that "a liberal equitable subrogation doctrine can save billions of dollars by reducing title insurance premiums. Title insurance primarily insures there are no intervening liens, and when a jurisdiction adopts the liberal view of equitable subrogation, the insurance premium is greatly reduced. . . We have demonstrated that title insurance costs in residential mortgage refinancings represent billions of dollars annually – costs that are now borne overwhelmingly by homeowners." Id. at par.33. The court further stated that "A liberal approach is in line with the [equitable subrogation] doctrine's equitable rationale and is becoming the more acceptable rule, in no small part because of the immense benefits it holds for homeowners." Id. at par. 34. The court concludes, after examining the existing case law, that "[t]his trend is clearly toward the more liberal [Restatement] approach, and we would be wise to follow it." Id. at par. 27. Also the court, in discussing the "history of equitable subrogation," stated at par. 24:

The rule requiring a subrogee have no knowledge of intervening interests is left over from an early mistrust of equitable subrogation and was borrowed from courts applying subrogation as a restitution remedy. We abandon this rule since this early mistrust has abated, and we are concerned with refinancing mortgages, not restitution.

Note also footnote 19, which states that: "Lest anyone fear for the future of the title insurance industry, Professors Nelson and Whitman assure us "the title insurance industry can endure a significant reduction in refinance premiums (citation omitted). Additionally, Nelson and Whitman spoke with a variety of executives representing major title insurance companies and mortgage lenders from all geographic areas of the country . . . Their comments were unanimous in one important respect – they supported either judicial or legislative adoption of the Restatement subrogation rule (citation omitted)." Id. at fn.19.

Finally, the court listed two "policy considerations" that it alleges support its position that the Restatement approach should prevail: "First, by facilitating more refinancing, equitable subrogation helps stem the threat of foreclosure . . . Second the Restatement approach affords enormous financial benefits for many homeowners." Id. at par. 32-33.

The dissent in this case argues that the refinancing mortgagee should be protected only if it has actual knowledge of the intervening lien. The dissent reasons that "in my view a commercial lender who undertakes no title search will be unable to demonstrate, as the Restatement (Third) requires, that it 'reasonably expected' to receive a security interest in the real estate with the priority of the mortgage being discharged" (citation omitted) (emphasis in text). Id. at par. 41.

See also footnotes 9-11, which contain a good summary of the case law on this issue in various other jurisdictions.

Reporter's Comment 1: The court's opinion in the *Prestance* case is certainly thorough and well researched and reasoned; but the Restatement approach is still (as the court notes) not the "majority" ruling in these types of cases (although the court, after examining the case law on this topic, states that the "trend" in recent cases is toward the Restatement approach).

Reporter's Comment 2: The decision has almost no discussion regarding the distinction that other cases make between "conventional" and "equitable" (or "legal") subrogation. In this regard, the court itself may be confused by the distinction and states only that "We agree with the Restatement at least in the context of a conventional refinancing. A lender providing funds to pay off an existing mortgage expects to receive the same security as the loan being paid off." Id. at par 27.

Reporter's Comment 3: With respect to mortgage loans, the doctrine of equitable subrogation generally provides that when loan proceeds from a new loan are used to satisfy a prior lien, the new lender stands in the shoes of the prior lienholder, if there is no prejudice to other lienholders. It rests on the equitable maxim that no one shall be enriched by another's loss, and may be invoked when justice demands its application. The doctrine is designed to prevent an unjust forfeiture, on the one hand, and a windfall amounting to unjust enrichment, on the other. But many courts apply the doctrine of "conventional subrogation," a fraternal — but not identical — twin of equitable subrogation, and allow claimants to bypass equitable defenses that have operated to defeat subrogation claims in the past. See, e.g., *Aames Capital Corporation v. Interstate Bank of Oak Forest,* 315 Ill.App.3d 700, 706 (Ill. App. 2nd Dist. 2000):

"There are two broad categories of subrogation rights: contractual or conventional rights, and common-law or equitable rights. *Schultz v. Gotlund*, 138 Ill.2d 171, 173 (1990). Equitable subrogation is a creature of chancery (a court of equity) that is utilized to prevent unjust enrichment. There is no general rule that can be laid down to determine whether a right of equitable subrogation exists, since the right depends upon the equities of each particular case. (Citing *Dix Mutual Insurance Co. v. Framboise*, 149 Ill.2d 314, at 319 [1992].) Conventional subrogation, on the other hand, arises from an agreement between the parties that the subrogee pay a debt on behalf of a third party and, in return, be able to assert the rights of the original creditor. *See Home Savings Bank v. Bierstadt*, 168 Ill. 618, 624 (1897)."

Noting that "[t]here are no Illinois cases of recent vintage that explain when subrogation will apply to a mortgage refinancing," the appellate court nonetheless observed that "[t]here are numerous policy reasons to apply the doctrine of conventional subrogation to a case involving a refinancing mortgage." Id., 315 Ill.App.3d at 709.

But the doctrine of equitable subrogation also has ancient origins and the law is well developed in this area (if not to a great extent in Illinois). Both the "conventional subrogation" and "equitable subrogation" doctrines are creatures of equity, and the court may be creating a distinction without a meaningful difference. In addition to Illinois, the court in *Aames* lists other state (and federal) jurisdictions that recognize the "conventional subrogation" doctrine.

See also *LaSalle Bank, N.I. v. First American Bank*, 316 Ill.App.3d 515 (Ill. App. 1st Dist. 2000), where the court also expressly affirmed the doctrine of conventional subrogation. According to the court:

[I]n terms of real property, the doctrine of conventional subrogation holds that when a refunding mortgage is made, the lien of the old mortgage continues in effect without interruption and the refunding mortgage does not become subordinate to an intervening lien or interest attaching between the time the old mortgage was recorded and the effective date of the refunding mortgage, even though the old mortgage has been released. (citations omitted.) Id. at 521.

And see *Welch Foods, Inc. v. Chicago Title Insurance Co.*, 341 Ark. 515 (Ark. Sup. Ct. 2000), where the court stated that:

"Conventional subrogation, as the term implies, is founded on some understanding or agreement, express or implied, and without which there is no "convention."' *Courtney v. Birdsong*, 246 Ark. 162, 437 S.W.2d 238 (1969). Legal or equitable subrogation, on the other hand, is a creature of equity, and not dependent upon contract, but rather dependent upon the equities of the parties. It arises by operation of law." Id. at 519

Reporter's Comment 4: Title insurers have legitimate concerns regarding court decisions on equitable subrogation. Whenever a title insurer pays a claim, it will ask the claims handler to consider possibilities for recovery from someone who may have been unjustly enriched. Often this inquiry begins and ends with consideration of the title company's rights under the legal doctrine of "equitable subrogation." When it works as intended, this doctrine allows the insurer to stand in the shoes of the injured party (the insured) and sue for recovery from any other party who, in equity and fairness, should pay for the problem. But some courts have proven themselves inhospitable to such suits, for various reasons — particularly where the claim is seen as resulting from some mistake by the title company's employee or agent.

In a case from the State of Washington Supreme Court, *Kim v. Lee*, 31 P.3d 665 (2001), discussed (and distinguished) by the Washington Supreme Court in the *Prestance* case, *supra*, the judgment lien holder filed to execute on his judgment lien and the title insurer intervened to protect its insured lender. The title company had failed to discover the judgment lien when it searched title, and even though Kim made the company aware of it prior to closing, the title company closed without paying off Kim's judgment lien. The majority opinion states: "Under the Restatement [of Property 3d: Mortgages], a modification of a mortgage will ordinarily cause it to lose priority to junior interests to the extent that the modification is materially prejudicial to those interests. Absent an increase in the principal amount or the interest rate of the mortgage, such modifications normally do not jeopardize the mortgagee's priority as against intervening interests." The court also found that the modification of the loan repayment term from 6 years to 30 years and the fact that this was a new mortgage were materially prejudicial to Kim, the junior lien holder. The court also refused to allow equitable subrogation where, as in the Kim case, the party seeking subrogation had actual knowledge of the intervening interest. The court then described the role of the title insurer, saying: "Generally, the role of the title insurer is relied upon by the lender, judgment creditor, and other lienors. Just as a lender relies on the title insurer to commit that title is vested in its borrower, subject only to known exclusions, judgment creditors and other lienors rely on title insurers to prevent a debtor from conveying real property without first satisfying a perfected lien. In the instant case, legal remedies and equity suggest that the loss should fall on the title company rather than the innocent judgment creditor." The court summarized its discussion of the equitable subrogation doctrine by saying: "Although the doctrine of equitable subrogation may be applied, this case is controlled by *Coy v. Raabe*, 69 Wn.2d 346, 418 P.2d 728 (1966), which allows equitable subrogation to a *bona fide* purchaser (or refinance lender) to the extent they were entitled to rely on others to guarantee title. However, equitable subrogation should not apply in favor of a title company, which guaranteed title while on constructive or actual notice of a prior judgment."

This is simply incorrect! A title insurer does not "guarantee" title; it insures the title to the property subject to the terms, conditions, exceptions and exclusions contained in the policy. Furthermore, the title insurer itself did not have a lien on the property, its insured lender did, and the lender and not the title insurer would be the direct beneficiary of any right to equitable subrogation! Also, it is at least a stretch to say that title insurers owe duties to third parties with whom they are not in privity or bound by any contractual relationships. Finally, the court's assertion that permitting equitable subrogation when the title insurer has actual or constructive notice effectively prevents any lien holder (or judgment lien creditor or any other party with an interest in property) from being entitled to the benefits of equitable subrogation whenever that party has title insurance, while those that do not have title insurance will be allowed such benefits. The court in Houston v. Bank of America, 119 Nev. 485, 489 (Nev. Sup. Ct. 2003), specifically rejected this approach, noting that, "precluding equitable subrogation when a mortgagee discovered or could have discovered a junior lien runs contrary to the purposes underlying the doctrine."

Reporter's Comment 5: The majority (though slender) view of equitable subrogation in the United States is still that the equitable subrogation doctrine is only available if the party paying the prior lien has no actual knowledge of the intervening lien. The Restatement (Third) of Property

(Mortgages) seeks to expand the right of equitable subrogation, and provides that a refinancing lender is equitably subordinated to the priority of the first mortgage even where it has actual knowledge of the intervening lien:

"Under this Restatement, however, subrogation can be granted even if the payor [the refinancing lender] had actual knowledge of the intervening interest; the payor's notice, actual or constructive, is not necessarily relevant. The question in such cases is whether the payor reasonably expected to get security with a priority equal to the mortgage being paid. Ordinarily lenders who provide refinancing desire and expect precisely that even if they are aware of an intervening lien. A refinancing mortgagee should be found to lack such an expectation only where there is affirmative proof that the mortgagee intended to subrogate its mortgage to the intervening interest. Restatement (Third) of Property: Mortgages § 7.6 cmt.e (1996)"

The more liberal Restatement position is, as noted earlier, not yet the majority view. In any event, there are prudent steps that a real estate practitioner who represents mortgage lenders can take to avoid the loss of priority of a new mortgage, where some or all of the proceeds from the mortgage are intended to be disbursed to pay off a prior recorded mortgage. Obviously, the mortgage loan documents should — and almost always do — clearly state the intention of both the mortgagor and the mortgagee that the mortgagee is to receive a properly perfected first mortgage lien against the property. If the parties are aware of an existing mortgage lien, it also would be beneficial to state in the loan documents that it is their intention that the new mortgagee is to receive the priority of that existing mortgage (if it is not to be released). The new mortgagee's attorney should obtain a title commitment to ascertain the status of title and to determine if there are any presently existing mortgage liens or other encumbrances against the property (and whether there are any subsequent liens or encumbrances appearing thereafter), and a title policy insuring the new mortgagee's security interest as a prior, valid and enforceable first mortgage lien on the property. (The availability, extent and scope of such coverage will depend on the facts and circumstances of each transaction, as well as underwriting considerations based on applicable case law and title insurance regulations; title insurers have recently issued new title products that greatly decrease the cost of title insurance in connection with mortgage refinancings). The refinancing mortgagee's attorney may also find it beneficial to have the existing mortgage lienholder, whose loan is to be paid off from the proceeds of the new loan, assign the existing mortgage to the new mortgagee (in those situations where there are intervening lienholders or encumbrancers) instead of releasing the mortgage from record (or at least leave the existing mortgage of record until the new mortgagee's loan is paid in full). Another prudent action would be to require, as a condition to the new mortgage loan, that any known or identified intervening lienholder execute (and agree to have recorded) an intercreditor or subordination agreement, whereby the intervening lienholder would consent to the new mortgage lien and confirm that its lien would be subordinate to the new mortgage (at least to the extent of the outstanding amount of the prior lien being paid from the proceeds of the new loan).

As to the key issue of the scope of equitable subrogation (and its offspring, "conventional subrogation"), litigation is often necessary to determine whether a mortgage lender who has paid off a prior lien is entitled to the priority of the earlier recorded lien. The goal of the actions mentioned above is to avoid, at all costs, a court challenge to the priority of the new refinancing mortgage. Decisions in this area of the law generally are highly fact-specific and uncertain, and mortgage priority disputes can be time-consuming and expensive for mortgage lenders to resolve. The resolution of such litigation often depends on off-record facts that are difficult to determine and prove — and meanwhile, title to the property remains undetermined and "in limbo" until the litigation is concluded. See generally, David H. Cox and Vernon W. Johnson III, State Equity Doctrine Helps Title Insurers, The National Law Journal, p. B17, Feb. 7, 2000.

It appears that the court in each of the cases discussed in these comments is trying to avoid any fact-intensive weighing of the equities, by setting up conventional subrogation as a "rule" to be followed. However, many state courts rely on equitable arguments to justify the rule. Although the cases discussed above involve different fact situations, it seems reasonable that a court should be able to find a "convention," sufficient to invoke conventional subrogation whenever a refinancing lender can show that it intended to pay off the senior debt (whether or not it had actual or constructive knowledge of the intervening lien), and that in exchange it intended to obtain a first mortgage. Otherwise, the doctrine of equitable subrogation, as interpreted differently by different courts, fosters uncertainty and unpredictability with respect to mortgage priority issues, and "clouds" real property records (and creates headaches for title insurers). Most real estate practitioners (and title insurers) would prefer real-property priority and recording rules that are clear and consistent. The only certainty at present may be that there is still some uncertainty as to how state courts (and bankruptcy courts construing applicable state law) will rule on this issue. As Professors Nelson and Whitman point out, without a clear and universal rule to follow, such as the Restatement approach, equitable subrogation is, quintessentially, a factual inquiry and its application is dependent on the facts and circumstances of each case and the jurisdiction where the case is decided.

Editor's Comment: For another recent case apparently adopting the Restatement approach, albeit in a remanded case, see ***Golden Delta Ent's. v. U.S. Bank, 213 S.W. 3d 171 (Mo. App. 2007).*** But compare ***Ethridge v. TierOne Bank,*** *2007, Westlaw 1816853 (Mo. 6-26-07)* incorporated under the heading: "Marital Property; Tenancy by Entireties; Mortgages." For a recent case rejecting the Restatement, see *Countrywide Home Loans, Inc. v. First Nat'l Bank of Steamboat Springs, N.A.*, 2006 Wyo. 132, 2006 Westlaw 2946869 (Wyo., Oct. 17, 2006)., the DIRT DD for 11/8/06. (Wyoming holds that institutional lender is not entitled to benefit of equitable mortgage doctrine where State has explicit "filing date priority" or "first in time" statute and lender has actual and constructive notice of intervening mortgage.)

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

MORTGAGES; VALIDITY; TENANCY BY ENTIRETIES: Where deed of trust states, in its granting clause, that it is given by a named individual, a married man, but the property at the time is owned in tenancy by the entireties, when the individual dies and his spouse's survivorship right takes effect, the deed of trust disappears, *even though the surviving spouse in fact executed the mortgage and benefitted from the expenditure of the proceeds.* ***Ethridge v. TierOne Bank, 2007 Westlaw 1816853 (6/26/07),*** Marital Property; Tenancy by Entireties; Mortgages."

MUNICIPAL AGENCIES; TELECOMMUNICATIONS: City's requiring connection of all new construction to city's broadband telecommunications system is an unconstitutional taking. ***Home Builders Ass'n v. City of Lebanon, 854 N.E.2d 1097 (Ohio App. 12 Dist. 2006), appeal den'd 854 N.E. 2d 1097 (8/2/06)***, discussed under the heading: "Constitutional Law; Due Process; Takings; Regulatory Takings."

NUISANCE; AIRPORT NOISE: Noise from aircraft flying within navigable airspace did not constitute a nuisance. ***Biddle v. BAA Indianapolis, LLC, 860 N.E.2d 570 (Ind. 2007)***, reported under the heading: "Eminent Domain; Inverse Condemnation; Airport Noise."

NUISANCE; STORM WATER RUNOFF: Storm water drainage can give rise to a prescriptive easement, but such an easement is limited in both location and scope to that occurring during the period over which the easement is acquired, and the reasonableness of a landowner's use of land must be assessed against the harm caused to adjacent property and the availability of remedial measures. ***Trenz v. Town of Norwell, 861 N.E.2d 777 (Mass. App. Ct. 2007).***

Claimants lived on a public street in the Town of Norwell (the "Town") and across the street from Meachem. The Town had installed four storm water culverts beneath the street, which culverts drained water onto Claimants' property. Meachem's property contained a pipe also directing rainwater into the culverts and subsequently onto Claimants' land.

Claimants brought suit alleging storm water runoff from the culverts was causing property damage and constituted a nuisance. The trial court found that because all relevant drainage fixtures were older than twenty years, a prescriptive easement had been created.

The trial court also found that use of the culverts had been reasonable, and that the runoff was a downhill flow, and the culverts were therefore not a nuisance. The court of appeals first addressed the nuisance issue. Citing *Tucker v. Badoian* (1978) 376 Mass. 907, the Court noted that fact finder must evaluate a landowner's activity for its effect on the flow of surface waters and the effect of that flow on others' land as compared to feasibility of remedial measures.

The Court noted this test requires a specific assessment of facts and weighing, which was not detailed in the trial court's decision.

Turning next to the issue of prescriptive easement, the Court found that even assuming a prescriptive easement had been obtained, such an easement would be limited in scope to its historical use. As such, the Court noted any modifications to the fixturing causing increased water flow would not be allowed by the easement. As the Town cited easement as its defense, the burden lay with the Town to prove existing use is consistent with the historical scope of the flow of water. The judgment was vacated and the case was therefore remanded for further findings into modifications made to the land over time, the practicality of remedial measures, and the scope of any easements.

OPTIONS; PRIORITY; "RELATION BACK:" Evidence that optionee had obtained title to optioned property was not sufficient to extinguish intervening mechanics' lien absent evidence optionee's title was obtained under the option. Optionee must demonstrate that it could have obtained specific performance of the option in order to show necessary relationship to get benefit of "relation back" doctrine. ***Wachovia Bank v. Lifetime Indus., Inc. 145 CA4th 1039, 52 CR3d 168 (2006)***

In 1993, Kmart sold an estate for years in property (Property) to Shawmut Bank and deeded the remainder interest (Remainder) to FGHK; FGHK sold Shawmut Bank an option to purchase the Remainder (Option Agreement) on the occurrence of specified events; Shawmut Bank mortgaged its interest in the Property (Deed of Trust) and assigned its interest in the Option Agreement to The Bank of New York.

In 2002, Lifetime Industries, Inc. (Lifetime) recorded a mechanics' lien against the Property.

In April 2003, The Bank of New York assigned its beneficial interests under the deed of trust to Wachovia Bank as the asset trustee for the property acquisition trust (PAT). At a 2003 foreclosure sale under the deed of trust, PAT purchased the estate for years and the rights of the optionee under the Option Agreement.

In January 2004, Lifetime obtained a judgment against FGHK providing for an award against FGHK, a lien on its ownership interest in the Property for the amount of the award, and an order that FGHK's interest in the Property be sold at public auction to pay the sums owed. In February 2004, when PAT notified FGHK of its intent to exercise the option to purchase the Remainder, FGHK asserted that PAT had breached the Option Agreement (by failing to protect the Property against the mechanics' lien) and was not entitled to specific performance.

PAT sued Lifetime and FGHK seeking, among other things, to quiet title. The trial court granted PAT's motion for summary adjudication of its claims against Lifetime.

The court of appeal reversed.

"An option to purchase real property is not a sale of the property, but a sale of a right to purchase the property. On exercise, the option is transformed into a contract of purchase and sale. When an option to purchase real property is exercised, the right to purchase the property relates back to the time the option was made. Until title is transferred, the optionee holds only a right to complete the purchase, enforceable by specific performance. Intervening interests, while subject to this right, are not yet extinguished. Furthermore, under the mechanics' lien law, once a lien is recorded, the lien will relate back to the date the first labor or material was furnished-for the work of improvement, and transferees who take an interest in the property after work has begun, and before the claim of lien is recorded, take subject to the lien." 145 CA4th at 1051.

Here, there was evidence to prove, or Lifetime did not dispute, that PAT held the option to purchase, the option was given and recorded prior to the date Lifetime first provided the labor or material for the work of improvement to which its mechanics' lien related, and PAT exercised the option to purchase on February 26, 2004. Nevertheless, the mere exercise of the option without consummation of the purchase and sale transaction did not provide PAT with title to the Remainder. Based on the record, title to the Remainder continued to be held by FGHK. Accordingly, Lifetime's lien against FGHK's interest in the remainder had not been extinguished.

The court denied PAT's CCP §909 motion to take evidence of a quitclaim deed from FGHK to PAT dated after the hearing on the summary adjudication motion.

PAT submitted no evidence that its receipt of the quitclaim deed was pursuant to its exercise of the option. If an optionee takes title to property when the optionee would not have been able to compel specific performance of the option, the relation-back rule does not apply, and the title obtained by the optionee does not extinguish intervening interests.

However, the court rejected Lifetime's argument that, under CC §2906, the exercise of the option, which was used as part of a financing transaction, could not relate back to the date of the option. Because the Remainder was not collateral within the meaning of §2906, the option, although granted to acquire an interest in the Remainder, was not granted to acquire an interest in real property collateral.

An option to purchase gives the optionee two significant benefits: First, as an internal matter between optionee and optionor, it can compel the property owner (the optionor) to sell the property later on, even though she might otherwise not want to sell. Second, externally, as long as the option is properly recorded, the title later conveyed pursuant to it relates back to the date the option was given and thereby takes priority over any intervening rights.

Thus, leases, contracts of sale, servitudes, and anything else created subsequently will be subject to the option- and may be lost when and if it is later exercised. The same is true for liens: Lifetime's mechanics' lien would be eliminated by PAT's paramount title if that title derived from the previously given option.

Reporter's Comment 1: There was no doubt that the option itself had been properly created, properly recorded, and, thereafter, properly exercised. Lifetime's strategy was to acknowledge these points, but declare them irrelevant because PAT's title assertedly did not derive from the option. It is true that any third party who acquired it from FGHK would take title subject to Lifetime's lien, without the benefit of any relation back. PAT exercised its option and it acquired title to the property, but did it acquire the title because it had exercised its option? Here, the court paraded some horribles

"Suppose, for example, that a condition to exercising an option to purchase property does not occur, or the optionee has breached the terms of the option agreement such that he cannot enforce the option, but the optionee nevertheless purchases title to the subject property in a new transaction wholly unconnected with the option. Under these circumstances, it appears to us that the purchaser should not have the benefit of the relation-back rule and his title should have no effect upon interests in the property that arose after the option and before the optionee's purchase."

Well, I guess that statement is true, but probably because the scales were loaded by making the new transaction "wholly unconnected." What if the final deal was only partly unconnected to the original one? In this case, the court was bothered by the fact that PAT took title by a quitclaim rather than a warranty deed, as the option called for, and by the fact that the conveyance was delayed because PAT was fighting with Lifetime over priority. If those two facts can disconnect a deed from its previous option, then holders of options must be extremely careful not to squander their priority. In this case, for instance, the option's reference to a warranty deed was obviously made by a New York attorney who neither practiced in California nor knew that such an instrument is effectively unknown here. Should California counsel, undertaking to complete the option purchase, attempt to draft such an instrument (with the attendant risks of using a nonform and untested document)? Or should she instead use a recognized California form, perhaps exposing her client to loss of relation back due to noncompliance with the terms of the option? Similarly, if there are deadlines in the option agreement that are jeopardized by external snags (here, the priority fight between PAT and Lifetime), should she advise the optionee to surrender to the third party in order to make the deadline, or dare she tell it that it can perform late as long as the optionor agrees (even if the third party doesn't)?

The court gives us the rule that relation back applies only when the optionee could compel specific performance, but I find that helpful only in an all-or-nothing context. In this case, for instance, neither party could specifically compel the other to deliver or accept a quitclaim deed, which makes it seem like there should be no relation back. Employing a hypothetical specific performance mini-trial to decide an issue between optionor and optionee seems like a dubious way to resolve a real priority contest between optionee and third party claimant.

The risk of losing relation-back status is not confined to option situations. All (but gift) deeds relate back to an earlier contract of sale, thus raising the issue of the priority of other claims that arise between execution of the contract and close of the escrow. In my experience, deals are more likely to be revised along the way than go from beginning to end without revision. The "relation back/specific performance" test thus puts the security and priority of a lot of transactions in question. Title opinions will have to do a lot of fudging.

I would have preferred a simpler standard. In *Meadows v Lee* 175 CA3d 475, 221 CR 22 (1985), where a court had to decide whether an original purchase contract that was performed late thereby lost its priority to a later contract sitting in backup position, the court employed a subjective test: Was the completion of the first contract "consummated between the original contracting parties in the absence of any showing of fraud or collusion as against third parties"? 175 CA3d at 483. That test is considerably more subjective than the *Wachovia Bank* standard. Under it, declarations from the optionor and optionee should be sufficient to warrant relation back unless the third party can show fraud or collusion. (I should note that the dissent in *Meadows* believed it a mistake to reach such a result "solely from the fact that the original parties are not presently disputing the validity of the second contract" (175 CA3d at 487), but the test clearly has the virtues of simplicity and certainty.) I suggest that in any transaction, the original parties-optionor and optionee, or whoever they are-accompany their closing with a joint declaration that it derives from their original deal (if that is true). That should matter considerably under the *Meadows* standard, and will certainly not hurt under what may be the more restrictive *Wachovia* test.

Of course, it would also be nice for an optionee or purchaser to give itself additional elbow room by providing in the original contract that it embraces all, e.g., alterations, revisions, extensions thereafter, if any such occur, borrowing from the way that lenders seek to preserve their priority despite subsequent modifications of their loan arrangements. But that takes forethought as well as consent of the other party, neither of which may be easy. Even then, how confident can their attorneys be that the language will work?

There is probably no way to provide 100 percent assurance that relation back will not be lost when the terms of a deal are altered. I guess the best we can do is be alert to the risk and hope for the best.

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RECORDING ACTS; *LIS PENDENS:* Filing of *lis pendens* with county recorder does not impart constructive notice until indexed, even if delivered to the recorder a week earlier. ***Dyer v Martinez 147 CA4th 1240, 54 CR3d 907 (2007)***

On September 9, 2004, Dyer sued the Rojases for specific performance and damages based on their alleged breach of a sales agreement for real property and, on the same day, deposited a *lis pendens* with the county recorder's office for recording. Although the *lis pendens* reflected a September 9, 2004, recording date, it was not indexed until September 14, 2004. On September 10, 2004, escrow closed on the sale of the property to Martinez, who purchased it through loans provided by Argent, secured by trust deeds that listed Town & Country as trustee.

Dyer filed an amended complaint for breach of contract, quiet title, and declaratory relief against Martinez, Argent, Town & Country (collectively, Defendants), and the Rojases, against whom she continued to seek specific performance. Defaults were entered against the Rojases. The trial court granted the remaining Defendants summary judgment on the ground that Dyer's *lis pendens* failed to provide constructive notice of her claim against the property, and ordered the *lis pendens* expunged. Dyer petitioned for writ of mandate directing the superior court to vacate its expungement order.

The court of appeal deemed the writ petition to be a notice of appeal from the judgment and affirmed.

"For more than a century, the law in California has been that a recorded document does not provide constructive notice to a *bona fide* purchaser of real property unless and until it can be located by a diligent title search, even if the literal wording of the relevant statute provided that the document imparted constructive notice from the date of filing with the recorder. To rely on the fiction of constructive notice and abrogate the requirement of actual notice, the party seeking recordation must ensure that all of the statutory requirements are met. Real property purchasers or mortgagees cannot be charged with constructive notice of documents they cannot locate;

thus, a *lis pendens* that is not indexed does not give notice because no one can find the document.

Nothing in the statute governing the recording of a lis pendens (CCP §405.24) indicates the legislature intended to abrogate the long-standing and uniformly applied rule that purchasers do not receive constructive notice if a diligent title records search would not locate the documents providing that notice. The statute provides that constructive notice is given only when an instrument is recorded, not simply when an instrument is delivered to the recorder's office. Given the history of constructive notice in California and the legislature's comment that enactment of §405.24 was not intended to change existing law, the term "recording" in that statute means "recorded as prescribed by law." Government Code §27250 requires indexing of all recorded lis pendens. Thus, a lis pendens does not provide constructive notice until it has been properly indexed."

Although failing to impute constructive notice until a *lis pendens* is indexed may create uncertainty because the claimant has no control over when the recorder indexes the document, the uncertainty would be greater if a purchaser of real estate could not rely on a diligent search of public records to reveal a prior claimant's interest. Placing the risk of loss due to a recorder's delay in indexing on the claimant provides an incentive to diligently deposit the lis pendens for recordation. Placing the risk on the innocent purchaser or the purchaser's title insurer does nothing to ensure the lis pendens is properly and timely recorded."

Reporter's Comment: The plaintiff had to lose this case if the recording system was going to work; otherwise, none of the rest of us could ever rely on the indexes. But reaching that common-sense outcome is made difficult by the fact that the literal language of our statutes seems to dictate a contrary result. Our *lis pendens* act provides that a recorded document gives constructive notice "[f]rom the time of recording" (CCP §405.24); "recording" is defined (in CC §1170) as meaning "deposited in the recorder's office, with the proper officer," without adding that the recorder's office had better next make appropriate index entries showing its location in the official records so that searchers can thereafter find it. A document not properly indexed should not be deemed recorded, even though it may have been left with the recorder (and even though it may also have been placed in the official records), since no one will ever come across it thereafter. Thank heavens our courts have gone activist on this issue and displaced the literal and unworkable statutory definition in favor of a functional one that makes recording depend on findability.

Not all courts are so bold. Last year, the Pennsylvania Supreme Court chose the literal version of the definition to conclude that a mortgage indexed under the wrong name nevertheless gave constructive notice to a subsequent party who had no actual knowledge of it because it had been properly delivered to the recorder's office. *First Citizens Nat'l Bank v Sherwood* 879 A2d 178 (Penn 2005). It took a considerable amount of work by the Pennsylvania Bar Association to get that statute amended to undo that result, by changing the statute to say that a document gives constructive notice only if it is "indexed properly."

The Pennsylvania court's decision may seem silly, but that is considered to be the rule in a majority of states, according to Patton & Palomar on Land Titles §68 (3d ed 2003). (While I am suspect of that count, because many of the citations are pretty old, it is a fact that the Idaho Supreme Court reached the same result just three years ago-Miller v Simonson (Idaho 2004) 92 P3d 537 – as did courts in Florida, Kansas, Louisiana, Vermont, and, more recently, West Virginia, where indexing is considered merely a ministerial act, according to Patton & Palomar.) More surprisingly, the drafters of Article 9 of the Uniform Commercial Code consciously take that same position. Section 9-517 provides, "The failure of the filing office to index a record correctly does not affect the effectiveness of the filed record." (Emphasis added.) (See also Com C §9517.) They say that mistakes don't happen that often and they don't want to overburden the filing office by having everybody coming back to double-check their filings, although that worry is rather hard for me to understand given the ability to computer search those files from one's own office.

Making life sensible for searchers, as this case does, comes at a price, however, and filers are the ones who will have to pay it. They will lose even if they have done everything right – *i.e.*, left the right document at the right office with the right fee-but a governmental clerk then failed to properly index it thereafter. Under a definition that deems a document recorded only when it has been properly indexed, the filing party has to double-check that this critical last step was done right.

In many cases, a search a few days later will show whether that was the case, but not always. Here, for instance, this plaintiff lost not because of a recorder's error, but because of its delay, in a situation where time was critical. The plaintiff had to get her *lis pendens* on file fast in order to stop a closing that was to occur the next day. (The facts are not clear, but I assume that the timing of her filing was not just coincidental.) Ignoring the merits of her strategy and claim, her problem is one that I do not know how to solve.

Government Code §27320 says that the recorder shall record any instrument deposited there "without delay," but I fear that means only copy it into the official records; the obligation to index it, in Govt C §27324, does not include the same time constraint. The Orange County Recorder's Office indexing delay of 5 days violated no statute. (The only other statutory speed mandate I am aware of is in CC §2941(c), where a two-business-day deadline is imposed on the recorder, but that only requires the office to "stamp and record" a satisfaction of mortgage form it receives in the mail.) A frantic filer can perhaps nag the recorder to move more quickly, but I doubt that she could get any judge to issue a writ to that effect. Possession can also give notice, so there is the possibility of the plaintiff camping out on the property, but that idea seems subject to the legal difficulty that a purchaser's obligation to look at the property may not require going there every day to do so (and the practical difficulty that a vendor in possession may not take kindly to the plaintiff's conduct).

In this case, because the plaintiff did appear to know that escrow was to close the next day, she probably also knew, or could have found out, who the purchaser was or where the closing was to be. Since actual knowledge is supposed to be a good substitute for the constructive notice furnished by an indexed lis pendens (see *Packard Bell Electronics Corp. v Theseus, Inc*. 244 CA2d 355, 363, 53 CR 300 (1966), perhaps a letter to the right place might also work. (I would caution her to use Federal Express rather than the U.S. mails if she really wants it to get there in time.)

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SERVITUDES; COVENANTS; LIABILITY: A successor-in-interest is only liable for those obligations imposed by an equitable servitude during the time the successor holds title. ***Clark v. Mead Realty Group, Inc., 854 N.E.2d 972 (Mass.App. 2006).***

Clarks agreed to sell a portion of their subdivided land ("Parcel A"), together with a small parcel providing an access to Parcel A ("Parcel B-1"), to Ampad Corporation in 1984. In the deed to Parcel B-1, the Clarks granted Ampad an option to acquire the remainder of their land ("Parcel B") anytime prior to January 10, 1990. The deed provided that if Ampad did not exercise its option prior to January 10, 1990, Ampad was to reconvey Parcel B-1 to the Clarks, subject to Ampad's right to continue to use the road and utilities installed on Parcel B-1, and Ampad was to construct a road and water line across Parcel B. The deed language stated specifically that the property was subject tot he terms of the option agreement.

The Clarks filed a complaint against Ampad in 1992 for breach of contract, waste, trespass and for specific performance under the option agreement for failure to perform. The Clarks received a temporary order enjoining Ampad from conveying Parcel B-1 but the motions lapsed in 1998.

Later in 1992, Ampad conveyed a portion of Parcel A and all of Parcel B-1 to Mead.

The Superior Court dismissed the complaints against Ampad for a declaration that Ampad had exercised its option or that Ampad should be estopped from denying its exercise.

After Ampad filed for bankruptcy in 2000, the Clarks filed a complaint against Mead for declaratory and injunctive relief based upon the following claims: (1) Mead was bound by the earlier agreement under an equitable servitude; (2) Mead was in breach of contract for failure to reconvey Parcel B-1 or construct the improvements on Parcel B; (3) alleged trespass or nuisance for discharge of water onto Parcel B-1; (4) *de facto* exercise of the option agreement; (5) declaration of constructive trust for the value of Parcel B-1 and an accounting of all financial benefits; (6) unfair and deceptive trade practices under Massachusetts General Laws, Chapter 93A ("Chapter 93A"); and (7) civil conspiracy with the city in the city's taking of Parcel B-1 and a portion of Parcel A.

Mead won summary judgment with regard to the breach of contract, *de facto* exercise of option and civil conspiracy claims. A jury trial found for Mead regarding the trespass and nuisance claim, and after dismissing the jury, the trial judge found for Mead on the declaratory and injunctive relief and constructive trust claims. The Clarks appealed.

With regard to the equitable servitude argument, the trial judge found that the deed to Ampad from the Clarks burdened Parcel B-1 by using the language "subject to" the agreement. Because the deed did not state that it was to bind successors in interest, the court applied what it characterized as the "default property rules" set forth in the Restatement of Servitudes, Section 4.4(1). This rule states that, unless the covenant clearly so states, a successor is only liable for obligations that accrue when that party holds title. Ampad's obligations arose two years prior to Mead acquiring the interest in the property, and therefore Mead was.not liable.

The court also rejected Clark's other arguments that would have imposed liability on Mead. With respect to the claim on the Unfair Business Practices Act, the Appeals Court found the Clarks' claim was time barred as it was more than four years after the alleged wrong. The ongoing injuries are not sufficient to extend the statute of limitations. In any even, the court said, Mead had no liability, as described above. .

Comment 1: Plaintiff's argued that it was obvious that the purpose of the covenant was to bind whoever was in title to the property to reconvey the property if the option was not exercised. Otherwise, the covenant could easily be circumvented by transfer of title, as happened here. It is not crystal clear from the opinion, but Mead may in fact have owned all the stock in the Ampac at the time of the transfer to Mead, thus making more telling the charge that this was all a conspiracy to strip Clarks of their rights. Clarks delay in eight years in pressing their claims, particularly after letting a preliminary injunction lapse, likely did not put them in as strong an equitable position as they would have liked on these issues.

Nevertheless, can it be doubted that any party taking with knowledge of Clarks rights to demand a reconveyance was not equitably bound to carry out that reconveyance? Apparently the court could doubt it, and did.

Was this the result that the Restatement had in mind? It does say that the parties must make their intentions clear if they wish to bind subsequent takers to perform covenants already breached when the transfer to such takers occurs. But why doesn't the language that the "land was subject to the agreement" sufficiently make clear that intent, at least when the equities seem to militate for such result?

Comment 2: On the other side of the argument, there is the notion that clear rules and clear default notions are in fact good for land transactions, as the parties have a rule book so that they know what to say and when to say it. The downside is that parties not fully familiar with the rules can get hung, as here, on a technicality.

Comment 3: Certainly Massachusetts lawyers should be fully aware today that their courts were going to take the Restatement of Servitudes seriously. But would this have been true in 1992? As the Restatement in fact is not really a restatement, but rather a new set of policy based rules in many respects, perhaps the courts should be more careful in imposing its technical requirements on transactions entered into before the Restatement was a reality.

SERVITUDES; RESTRICTIVE COVENANTS; BUILDING RESTRICTIONS: GARAGES: Restriction permitting the construction of a dwelling unit and a "private garage for not more than three cars" restricts only the number of cars, and a lot owner under the restriction could build more than one garage, but only if all garages had collective capacity for not more than three cars. ***Johnson v. Dawson, 856 N.E.2d 769 (Ind. 2006),*** also discussed under the heading: Servitudes; Restrictive Covenants; Enforcement; Waiver."

Plaintiffs sought to enjoin the construction of a new detached two car garage on a property within their subdivision. The subdivision covenants specified that "[n]o structure shall be erected, altered, placed or permitted to remain on any residential building lot other than one detached single-family dwelling not to exceed two stories in height and a private garage for not more than three cars." *Id.* at 773.

In addition to the proposed detached garage, Defendants' lot already contained an attached two- car garage. Plaintiffs argued that only one garage per lot was permitted under the Covenants. Noting that covenants are a type of express contract, the Court found that they are to be strictly construed and that ambiguous provisions should be construed ion favor of the free use of land.

Here the Court found the covenant to be clear as to the number of cars for which a garage could be constructed but ambiguous as to the number of garages allowed. In rejecting Plaintiffs' argument that the covenant allowed for the construction of only one garage per lot, the Court noted the contrast between the language allowing for "one detached single-family dwelling" and the relatively ambiguous provision as to "a garage." Concluding that the description of the garage in the singular was not indicative of the parties' intent to restrict the number of garages, the Court agreed with the trial court that the intention of the covenants was to limit the number of cars for which garages may be erected and not the number of garages. Accordingly, while the erection of a second garage on Defendants' property was not a *per se* violation of the Covenants, erection of the garage such that total garage capacity on the lot exceeded three cars did violate the Covenants.

Comment: Although the court found for the plaintiffs here, this almost became a very anti- covenant decision. The editor does not agree that the probable intent of the parties was to permit more than one garage, but rather to restrict the size of the single permitted garage to three car capacity. He feels that the presumption against ambiguous covenants was almost taken too far here.

SERVITUDES; RESTRICTIVE COVENANTS; PUBLIC HOUSING PROGRAMS: Where city sells property at bargain price subject to language implicitly restricting use to one- four family housing, covenants will run with the land to successor. ***328 Owners Corp. v. 330 West 86 Oaks Corp., 8 N.Y.3d 372, 834 N.Y.S.2d 62 (2007).***

City obtained through tax foreclosure a five-story townhouse serving as a multiple dwelling with eight units. The building had violations against it and under the city's asset sales program it was sold to the tenants – by means of a corporation they formed – as an Urban Development Action Area Project . The price was based on the capitalization of income instead of market value, which made it a bargain at $340,000.

The city imposed conditions on the sale that required repair of the various code violations, and limited the rent (presumably to any non-owner tenants) for two years. These conditions were in the deed and in documentation of the various approvals required under Projects of this type. The recitals at the beginning of the deed stated: "[T]he project to be undertaken by Sponsor ('Project') consists solely of the rehabilitation or conservation of existing private or multiple dwellings or the construction of one to four unit dwellings without any change in land use permitted by existing zoning. . . ." The deed also recited an intent that at least some of the covenants would run with the land: "The agreements and covenants set forth in this Deed shall run with the land and shall be binding to the fullest extent permitted by law and equity. Such covenants shall inure to the benefit of the City and shall bind and be enforceable against Sponsor and its successors and assigns."

Less than two years later, and without having corrected the code violations, the corporation sold the property to Buyer – for $1 million (or more – newspaper reports suggested a price of $2.2 million." Buyer planned to build a "sliver" high rise multi unit apartment building on the property. Presumable such use would have been permitted by existing zoning.

A neighbor, the owner of an adjacent building, which shared a party wall, brought an declaratory relief and injunction action against Buyer seeking a declaration that buyer the "four unit" restriction bound Buyer. The City joined the suit. City and neighbor alleged that the property was subject to a four unit limit for new development, and that this obligation, as well as the obligation to repair the code violations and to maintain rents to existing tenants ran with the land. Although the four unit restriction was not stated specifically in the deed, the reference to the City's Project, the petitioners argued, gave notice that other terms of the bargain sale more explicitly bound the owners to conserve the existing building and to limit any new construction to one to four units.

The court stated that three conditions must be satisfied for a covenant to run with the land, and found all of them satisfied here:

1. the grantor and grantee (of the original deed) must manifest an intent that it so run;

2. the covenant must touch or concern the land; and

3. there must be "privity of estate" between the one claiming the benefit of the covenant and the one against whom it's now sought to be enforced.

The neighbor, of course, lacked privity. It was not a party to the sale and was not linked to the chain of title. But the city had joined the suit, and therefore the court found the neighbor's lack of privity to be "immaterial."

Buyer emphasized that the covenants containing the restrictions were in the "recital" provisions of the deed rather than in its "habendum" clause, and therefore were invalid as restrictions on title. The New York Court of Appeals dismissed the distinction between the clauses and read the instrument as a whole in order to discern the parties' intent. In fact it was so instructed by a New York Statute.

The real dispute in the case, which split the court, and which had motivated the lower court of appeals to find against the city, was the question of whether the parties evinced an intent that the covenants run beyond the original purchasers.

The dissent, by Judge Pigott, argued that the intent of the restrictions on the use of the land for a four unit apartment building was to limit only the original grantee. He argued that otherwise the restrictions would have bound the property "in perpetuity," and that this was inconsistent with the transferability of the property. He pointed out that the language of the restriction on land use specifically referred to "the Sponsor." As to the "boiler plate" language about the covenants running, the judge noted that there were other covenants dealing with non discrimination that clearly did run.

The real question had to do with the four unit restriction. It appears that Judge Piggot agreed that the covenant relating to cure of code violations did bind the successor, but of course any code violations would be resolved when the property was demolished and the "sliver" building was erected. Judge Piggot's views apparently mirrored those of the lower appeals court majority, which had denied relief.

The majority countered that the restriction on land use could later be waived by the City, and therefore did not bind the property in perpetuity.

The City, relying again on the reference to the housing law relating to projects of this type, argued that the owners were required to conserve the existing building, rather than simply limit the use of the property to a one-four unit structure. The court denied this particular form of relief, holding that the reference to the general purpose of the statute was insufficient to impose such a restriction.

Comment 1: The vague and general reference in the deed to the purpose of the statute to provide for the rehabilitation of one-four family structures strikes the Editor as also unenforceably uncertain, and not a good basis for a covenant running with the land. The court seems to be of the view that various other contracts and approval documents were incorporated into the burdens imposed on the property, but it is very unclear exactly how it viewed this as happening.

But we should differentiate the original covenanting parties' purpose from the question of notice to successors. Here, prior to purchasing (if not prior to contracting) the proposed purchasers had adequate notice that there was a challenge based upon the overall preservation scheme. Therefore, arguably the question was not one of notice, but simply of interpretation of the original parties' intent.

Possibly a purchaser that had no express notice of the contents of the other land use agreements would not be put on constructive notice of them by the deed language. But don't bet the ranch on that – in fact the tenor of the opinion suggests that it would have found constructive notice, if necessary.

Comment 2: In the editor's view, the probable purpose of the City in fact was to bind successors. Otherwise, what was the point of the original deal? It would make little sense to sell a $2 million property to its occupants for $340,000 if there is no long term land use goal to be satisfied. The owners were already subject to code enforcement requirements. A two year rent cap does seem an insufficient additional objective to support the bargain price.

Comment 3: Note that the Court of Appeals resoundingly affirms most of the New York common law on the requirements for covenants running with the land – the touch and concern requirement and the "vertical privity" requirement. Note also, however, that the City was not the owner of "benefitted property." It appears that the court is implicitly acknowledging that covenants in gross will run in New York. It may be that earlier authority had already crossed this bridge.

SERVITUDES; RESTRICTIVE COVENANTS; USE RESTRICTIONS; "RESIDENTIAL ONLY:" A restriction that property shall be used for "residential purposes" does not restrict the use of the property for daily and weekly rentals. ***Scott v. Walker, 2007 Westlaw 1651138 (Va. 6/8/07)***

Scotts and Walkers owned adjacent properties in a subdivision. Both lots were subject to the same recorded restrictive covenant:

"LAND USE AND BUILDING TYPE: No lot shall be used except for residential purposes. No building shall be erected, altered, placed or permitted to remain on any lot other than one detached single-family dwelling not to exceed two and one-half (2 1/2) stories in height, a private garage for not more than two cars, boat dock and boat houses. No lot or lots in said subdivision can be re-subdivided except a lot may be subdivided providing each part is allotted to an adjoining lot."

Scotts began using the residence on their property for nightly and weekly rentals, and Walkers objected. This litigation ensued, and the trial court enjoined Scotts' activities, finding it in violation of the "residential purposes" restriction.

The Supreme Court of Virginia reversed, holding that the application of the "residential only " language to this type of use is sufficiently ambiguous as to invoke the principle that ambiguous land use restrictions ought to be construed in favor of free use of the land.

The court cited a number of cases from other jurisdictions and from Virginia that were very close to this case, including two former DIRT DD's: Compare *Yogman v. Parrott*, 937 P.2d 1019, 1023 (Or. 1997) (the DIRT DD for 9/9/970 (short-term rental of lot did not violate restrictive covenant requiring that the lot "be used exclusively for residential purposes"), with *O'Connor v. Resort Custom Builders, Inc.*, 591 N.W.2d 216, 220–21 (Mich. 1999) (the DIRT DD for 3/3/99) (interval ownership in a home violated restrictive covenant prohibiting use of a lot "except for residential purposes"). Readers can find both collected on the DIRT Website: www.umkc.edu/dirt

The court also had before it some interesting Virginia precedent. One case found that simply renting rooms, without providing board, was a "residential" use in compliance with a the applicable residential only restriction. Another found that a boarding house was a "business" and violated a covenant requiring residential use only, even though the owner and her family lived in the kitchen. *Compare: Persson Mokvist v. Anderson,* 942 P.2d 1154 (Alaska 1997) (DIRT DD for 3/26/98).(Bed and breakfast usage permitted under "residential use"where restrictive covenant limits property to "residential use").

The court found that the duration of the residential stay ought not to be a factor. If the use was essentially residential in character, and did not entail the operation of some other business, then the covenant could not be stretched to prohibit such use, in light of the general Virginia preference for construing covenants in favor of free use of the land.

Under our case law, a restrictive covenant of "substantial doubt or ambiguity" must be interpreted "in favor of the free use of property and against restrictions." . . . If the restrictive covenant at issue was intended to prevent the short-term rental of lots in the Harbor Village Subdivision, "it would have been easy to say so, and it would not likely have been left to the uncertainty of inference." Id. In the absence of language expressly or by necessary implication prohibiting nightly or weekly rentals, we find that the Scotts' short-term rental of their property did not run afoul of the restrictive covenant at issue. The Walkers did not carry their burden to establish that the terms of the restrictive covenant prohibited the activity to which they objected." (Citations omitted)

Comment 1: In *Yogman v. Parrott, supra,* the Oregon Supreme Court suggested that a servitude restriction limiting the use of property "exclusively for residential purposes" was inherently ambiguous on the issue of whether short term rentals were permitted. The Virginia court relied extensively on the analysis in *Yogman*, but neglected to note that, in addition, the use restriction in *Yogman* stated that "no commercial enterprise shall be constructed or permitted on the property" and the court found that this, also, was too ambiguous t apply to short term rentals.

Also see Mullin v. Silvercreek Condo., Owner's Ass'n, 195 S.W.3d 484 (Mo. Ct. App. 2006) (nightly rentals did not violate residential restriction.) *Catawba Orchard Beach Assn. v. Gasinger,* 665 N.E.2d 584 (Ohio App. 1996) (DIRT DD for 2/15/98) (short term rentals do not violate " private residences" restriction in servitudes, but case remanded for determination of whether short term tenants' use of subdivision's beach and recreational amenities violated requirement that amenities be used for "noncommercial purposes."

Comment 2: In sum, Virginia is in line with growing authority on the issue of short term rentals. Note that the Virginia precedent concerning boarding houses involved a use that was a bit more of a business than a simple "bed and breakfast." But the line is a bit squiggly with regard to that activity, and it is difficult to know where Virginia would come out.

For another interesting "residential use" case, see *Turudic v. Susan Estates Homeowners Association*, 31 P.3d 465 (Or.App. 2001). (the DIRT DD for 2/18/05) (Keeping of pet cougars was a "residential use" within meaning of covenants; and discretionary authority of association review for construction of cougar pen was limited to aesthetic or design requirement). The editor wonders whether the Virginia court would have come out the same way as Oregon on that issue.

SERVITUDES; RESTRICTIVE COVENANTS; ENFORCEMENT; WAIVER: Under Indiana law, a nonwaiver clause in a declaration of restrictive covenants to which there are multiple parties is generally enforceable. ***Johnson v. Dawson, 856 N.E.2d 769 (2006).***

Plaintiffs were residents of the Meadowbrook Subdivision No. 1 ("Meadowbrook"). They sought an injunction to bar construction of a detached two-car garage on the property of Defendants, also resident of Meadowbrook, after the proposed structure was approved by Meadowbrook's Board of Directors.

Plaintiffs claimed the proposed garage violated the Meadowbrook Covenants, Restrictions and Conditions promulgated and adopted in 1956 (the "Covenants"). The trial court granted the injunction and Defendants appealed. The Court of Appeals affirmed.

The first issue on review was the proper interpretation of the restrictive covenant in question. The court concluded that the covenant did restrict the use in question. This is discussed under the heading: "Servitudes; Restrictive Covenants; Building Restrictions; Garages." (And in the DD for 7/11/07)

The Court further concluded that Meadowbrook's Board of Directors lacked the authority to issue a binding approval of a nonconforming structure. As is common in these cases, unless the Declaration is specific that the sole right of enforcement is in the board, the court ruled that individual lot owners had an independent right to enforce.

Defendants next argued that Plaintiffs' claims were barred by their failure to object to prior violations of the covenant in question by other residents of Meadowbrook. As the Covenants contained a nonwaiver clause, resolution of this issue turned on the enforceability of that clause under Indiana law.

Noting that the enforceability of a nonwaiver clause in the multiparty context was an issue of first impression in Indiana, the Court determined that the nonwaiver clause in this case was enforceable. In reaching its conclusion, the Court found that nonwaiver clauses in the multiparty context are not materially different than bilateral nonwaiver clauses, which, under Indiana law, generally are enforced.

The Court also noted that Defendants had willingly entered into the Covenants, including the express nonwaiver clause. Noting an important public policy consideration, the Court found that "enforcement of the nonwaiver clause in the multiparty context allows prospective purchasers of property to rely on recorded restrictions and covenants." *Id.* at 775. After rejecting Defendants' final argument that the trial court had improperly granted Plaintiffs attorney's fees, the court affirmed the judgment of the trial court.

Comment 1: Although the cases are full of discussions making the point that restrictive covenants are contrary to free development of property and should be read narrowly, we are seeing an increasing number of cases taking these covenants more seriously, whether or not they include the boilerplate "narrow application" language.

Of course, upholding a nonwaiver clause isn't a broad reading of the provision, as it specifically applied here. But, again, there are plenty of cases concluding that a nonwaiver clause can itself be waived. On the other hand, it is difficult to make a "waiver by silence" argument in the face of a nonwaiver clause.

Comment 2: One assumes that if the parties seeking to develop their garage had done so, based upon approval from the Board, and with no objection from the neighbors, an estoppel might arise. Call it waiver, laches, or any other equitable name you want, but that situation is different than the one at hand, where the construction had not yet been completed when the objection was raised.

Comment 2: How does this doctrine coordinate with the doctrine of "changed circumstances," discussed not long ago in DIRT (DD for 6/5/07)? Under that doctrine, if the environment in (or, in some jurisdictions, around) the controlled area has changed from the time that the covenants were entered into so that it is unlikely that the benefits of the original scheme can be enjoyed, then the court will not enforce the covenants.

Obviously, the same basic fact pattern can support a "changed circumstances argument" as one supporting waiver. The lot owners permit their neighbors over time to breach the covenant repeatedly, leading to a situation where a number of lots are already out of conformance, so that enforcing it now on the lot in question would be meaningless. Presumably, again, this case does not speak to that situation.

STATE AND LOCAL TAXATION; ASSESSMENTS; UNIFORMITY: Pennsylvania trial court finds property assessment system used in many parts of the state to be unconstitutional as a violation of the uniformity principle. ***Clifton, Cranor, et al. v. Allegheny County, (Civil Div. C.P. Allegheny County, PA No. GD05-028638, decided June 6, 2007***

Common Pleas Judge R. Stanton Wettick, Jr., here declared that the present Pennsylvania system for real estate tax assessments is unconstitutional and produces "arbitrary, unjust, and unreasonable discriminatory results." He ruled in favor of the complaining homeowners and ordered Allegheny County to conduct reassessments of all properties to bring them into line.

The case of, analyzed the long history of Pennsylvania's assessment law. That law permits real estate taxes to be levied on assessed values established by the use of a base-year market value for an indefinite number of years. If this decision holds up on appeal, it will affect real estate assessments throughout the state of Pennsylvania.

Allegheny County uses 2002 as its base year. This means that real estate taxes for 2007 were determined by using the 2002 fair market value of the taxpayers' properties. Under that system, market fluctuations over the five-year period were not reflected in the assessments.

The decision pointed out the obvious. Property values change at different rates. Also, properties in high-value neighborhoods appreciate at higher rates than property values in low-value neighborhoods. To cite an example of the impact of the 2002 year base, consider the Woodland Hills School District, which includes Edgewood and Braddock. Their taxes were calculated using 2002 fair-market values, even though between 2002 and 2005 property values in Edgewood increased by approximately 36% while property values in Braddock declined by 16%. On average this would make for a discrepancy of 52%!

This decision reverberates throughout the state because at least 34 of Pennsylvania's 67 counties have not conducted a comprehensive county-wide reassessment within the 20 year period from 1985 to 2005. For example, in 2005, a Philadelphia owner of property with a fair-market value of $100,000 in the most over assessed quartile paid property taxes of at least $3,310; and the owner having a fair-market value of $100,000 in the most under assessed quartile paid taxes of no more than $1,418. Wettick stated: "Using income tax terminology, one out of every four Philadelphia property owners was in a tax bracket of at least 3.31% and one out of every four property owners was in a tax bracket that did not exceed 1.42%."

The judge also highlighted what he called a high "Price-Related Differential" of 1.18 which means that owners of less expensive properties are more likely to be over assessed, and owners of more expensive properties are more likely to be under assessed. This created unacceptable inequality to the judge.

"Constitutions of almost every state, including Pennsylvania, have Uniformity Clauses. Pennsylvania has consistently required equality of taxation under the Uniformity Clause, and based on long-established case law, this equality "is met only when, to the extent reasonably practicable, the ratio of assessed value to actual value is the same to every property."

The judge noted that absolute equality is not the goal. As earlier cases have held, only "approximate equality" can reasonably be expected. The body of case law on these issues provides that there must be substantial uniformity, which means as nearly uniform as practicable under all of the circumstances. The law must attempt to set up a system so that the burden of real estate taxes is shared by all owners fairly.

The County argued that a base year system does not violate the Uniformity Clause because an owner has a safety valve of appealing a base-year evaluation by applying the established common level ratio to the property's current market value .The court rejected that argument because it would place the burden on the taxpayer to equalize ratios. Also, a possibility of appeal does not work to equalize assessments because taxpayers who are under assessed will not be likely to file appeals to increase their assessments.

Reporter's Comment 1: Apparently, the main culprit is the Pennsylvania legislature. Pennsylvania and Delaware are the only states without requirements that assessments be based on current or relatively current actual values. The laws and regulations of 22 of the remaining 48 states provide for annual assessments. Nine of these 22 have specific requirements for periodic field reviews. The other 26 states provide for reassessments at intervals of more than one year. With few exceptions the period of time is between two and five years. Pennsylvania and Delaware also differ from other states because the other 48 states, unlike Pennsylvania and Delaware, have state agencies that exercise supervisory responsibility over the assessment programs of the different counties.

Reporter's Comment 2: Frequent reassessment would facilitate uniformity. Unfortunately, it would place a substantial burden and expense on municipalities that try to conform to this standard, instead of sticking with the base-year system generally used throughout the Commonwealth.

Reporter's Comment 3: A substantial part of the opinion is dedicated to a state-by-state analysis of assessment laws and constitutional amendments throughout the country that deal with uniformity and real estate taxes. This may be of only academic interest to Pennsylvania real estate practitioners, but it may prove to be a valuable guide if and when the Pennsylvania legislature ever gets around to honoring Judge Wettick's recommendations and attempts to bring tax uniformity into Pennsylvania. Based on his analysis Wettick concluded that more than half of the states have enacted assessment legislation that does not require annual reassessments. Virtually every state other than Pennsylvania has set up a state agency with oversight responsibility as a necessary feature of an assessment scheme designed to produce assessment uniformity and equality. Pennsylvania has not done this, but Wettick's conclusion is that courts should not have the duty to provide for alternatives to annual reassessments or to the kind of agencies that must be set up to accomplish these objectives. He feels strongly that these things are a matter for the legislature.

Reporter's Comment 4: Allegheny County will undoubtedly challenge the opinion and oppose the order to reassess all properties. The Pennsylvania legislature will probably ignore the recommendations for new legislation, at least for now.

Meanwhile, the impact of this decision on taxpayers must be carefully considered. Property owners in Philadelphia and elsewhere who think they are being unfairly assessed will undoubtedly be citing this Allegheny County case in attempts to achieve fairer assessments for themselves.

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STATUTE OF FRAUDS; EXTRINSIC EVIDENCE; PRICE: Although extrinsic evidence may be admitted to clarify ambiguous terms in order to establish that a writing satisfies the Statute of Frauds, the extrinsic evidence must in fact support language in the written agreement, and not substitute for it. ***Sterling v. Taylor, 40 C4th 757, 55 CR3d 116 (2007)***

Sterling wrote out a handwritten memorandum of her deal with Taylor for her to buy some of his properties for "approx 10.468 X gross income [,] estimated income 1.600.000, Price $16,750.00," and Taylor later signed another piece of paper acknowledging some of that. When Sterling later discovered that actual income from the properties was only $1,375,404 (not $1,600,000), she thought she should have to pay 10.468 times that, or

$14,404,841, whereas Taylor believed she should pay $16,750,000. Sterling sued for specific performance, but the trial court rendered summary judgment against her on the ground that the memorandum did not state the price clearly enough to satisfy the Statute of Frauds. (Remember, it was Sterling arguing that the price was $14 million. There was no argument that the price was in fact only $16,750.00. It seemed clear to all that this was not the price, and that the parties had misstated what was supposed to be $16,750,000.)

The court of appeal reversed, holding that extrinsic evidence could be admitted to clarify the price and satisfy the statute, but then the supreme court reversed the court of appeal and affirmed the trial court. In doing so, the high court unanimously said that it agreed with the intermediate court about the propriety of extrinsic evidence being used to enable an ambiguous memorandum to satisfy the Statute of Frauds, but then five justices went on to say "but not in this case." Sterling's extrinsic evidence was offered to support a $14.4 million price, which was nowhere in the contract, and did not support, for Statute of Frauds purposes, the $16.7 million price that was in the contract, a position that caused two of the justices to dissent to that conclusion and want to leave it for the trier of fact – rather than the supreme court – to decide.

Reporter's Comment: I don't want to look like I'm siding with the minority, but the problem I have with Justice Corrigan's majority opinion is that it does not give any guidance to attorneys who are attempting to predict intelligently to their clients the sufficiency of the writings that they have generated. An attorney lucky enough to draft the agreement herself can be expected, naturally, to assure that the documents she produces will not only correctly express the terms of the deal, but will also satisfy the Statute of Frauds. This is true as well when the memorandum sketched out by the clients themselves is given to her to critique or formalize. But if the fight has already started and the memorandum is all there is, and she needs to be able to tell the prospective plaintiff with some confidence whether to sue or give up (or to advise the defendant whether to fight or settle) based on that memorandum, then I fear that she will get no help from this decision. If the supreme court thought it was doing the bar a favor by giving it some guidance, I think it failed. I do not think that there is any constructive way for attorneys to correct their practices based on this decision.

Reporter's Comment 2: Some lesser parts of the decision will help practitioners. The holding that extrinsic evidence will be admitted to bolster the claim that the Statute of Frauds has been met is meaningful; an attorney no longer has to tell a plaintiff to abandon his claim because the document alone does not say enough, if there is enough additional supporting evidence to fill the gaps. Additionally, it is helpful to know that street addresses are good enough to satisfy the statute's requirement for specificity of subject matter (although I suspect that no one ever really doubted that point). Another aspect of the case that looked like it would have been a more serious Statute of Frauds question was that Taylor never signed the memorandum as the party to be charged. He did sign and send a letter 2 days later, but that letter contained no price term (and Taylor disputed that the earlier memorandum was attached to it); he also signed escrow instructions that showed a price of $16.7 million. I wish the court had explained how that took care of the absence of his signature on the memorandum.

Comment 3: But what takes the helpfulness away is the majority's final point that this extrinsic evidence – testimony that the formula was the real deal and the estimate only an estimate – would not satisfy the statute because the memorandum contained only the estimated number and not the formulaically derived one. The dissenters' objection-that the formula was as much included in the memorandum as was the estimate-sounds equally correct to me, but more important is the fact that the majority makes it so much harder for a practitioner to predict whether his or her client has a case. Under this new standard, when the writing alone is not sufficient, we must not only decide whether there is enough supporting evidence to get past the Statute of Frauds, but also whether that supporting evidence is sufficiently consistent with the writing – which is, by itself, admittedly ambiguous.

For instance, had Sterling come to me at the outset, I would have predicted that the writing seemed to give greater support to her formula ("10.468 X gross income"), worked out to 3 decimal places, than for Taylor's number ("Price $16,750.00"), a clearly rounded out figure with its three (rather than four) zeros at the end and no decimals, especially in light of the "approx" and "estimated" in the notes. If I had the luxury of choosing my client on this issue, I would have taken Sterling over Taylor, which would have been a bad call in light of what the majority said. (I should note that my conclusion also happens to be one that none of the justices took, perhaps another argument for requiring that the writing fill in the gaps in favor of one side of the dispute.) Luckily, we aren't asked too often whether incomplete writings satisfy the Statute of Frauds. While that issue now confronts more uncertainty than before, I daresay the bar will survive.

The Reporter for this item was Professor Roger Bernhardt of the Golden Gate Law School, writing in the California CEB Real Property Reporter. Reprinted and edited with permission.

STATE AND LOCAL TAXATION; ASSESSMENTS; UNIFORMITY: Pennsylvania trial court finds property assessment system used in many parts of the state to be unconstitutional as a violation of the uniformity principle. ***Clifton, Cranor, et al. v. Allegheny County, (Civil Div. C.P. Allegheny County, PA No. GD05-028638, decided June 6, 2007)***

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STATUTE OF FRAUDS; PROPERTY DESCRIPTION: Contract sufficiently describes the portion of vendor's land to be sold so that it doesn't violate the Statute of Frauds where it states that parties have agreed upon boundaries and later survey will provide exact description. ***Schuler v. Graf, 862 N.E.2d 709 (Ind. App. 2007)***, discussed under the heading: "Vendor/purchaser; Land Descriptions."

STATUTE OF FRAUDS; PAROLE GIFT OF LAND: Missouri courts will uphold a parole gift of land as conferring equitable title where the grantee takes possession of the property and other evidence indicates an intent to make a gift, but possession shared with grantor may not be sufficient to meet the possession requirement absent a very clear case of the grantor's intent. ***O'Dell v. Mefford, 211 S.W. 3d 136 (Mo. App. 2007)***

Mefford resided with owner of land and Bryan in a mobile home permanently affixed to the land for about four years. During that time, an assignment of ownership of the mobile home from Bryan to Mefford was recorded, but there was no record of a deed, and in fact no claim that a deed was ever executed. Later, alleged grantee moved out of the mobile home. Four years later, Bryan died and left the property to his sister by will. Mefford moved back into the mobile home about a month after the death, and the sister moved to quiet title against her.

The court noted that the mobile home had become a fixture, and ownership of it could not pass without a transfer of title to the land. It acknowledged that Missouri will recognize the validity of a parole gift of land to create equitable title in the land if the gift is accompanied by a transfer of possession. Although the court acknowledged that shared possession with the grantor may be enough to satisfy the transfer of possession requirement, there must be other clear and convincing evidence that a gift was intended.

Here the trial court did not find sufficient evidence of a gift. The appeals court noted that the evidence showed that Bryant had not signed the assignment of ownership of the mobile home, and Mefford's absence from the home for four years prior to Bryan's death also militated in favor of a conclusion that not gift had been intended.

TELECOMMUNICATIONS; CELL TOWERS; ZONING: A municipality that selects a telecommunications tower site for governmental use need only act reasonably in its site selection and, if its zoning ordinance exempts its sites from the need to obtain land use approval, it need not obtain such, even if its tower will be shared by private cellular service providers. ***Hills of Troy Neighborhood Association, Inc. v. Township of Parsippany-Troy Hills 392 N.J.Super. 593, 921 A.2d 1169, 2005 WL 3050995 (Law Div. 2005) , approved for publication April, 2007.***

A neighborhood association sought to enjoin construction of a municipal communications and telecommunications tower to be shared by the municipality and a cellular telephone company. The Court was presented with the issue of the "extent to which a municipality is exempt from its own zoning approval ordinances, the reasonable exercise of such authority and, to the extent so exempt, the novel question of whether private telecommunication companies may share in that exemption by co-locating on a communications tower on municipal property."

The municipality sought to replace a previous communications tower with one at the rear of its police station. The tower was to provide communications for essential municipal services. It also determined to lease a portion to cellular providers. It put the proposal out for bid, but prior to the opening of the bid, it submitted its plans for the replacement tower to a "courtesy review" by the municipality's planning board. The cellular company was the successful bidder and it applied for, and obtained, a zoning permit for the site. Negotiations resulted in a slight lowering of the tower's height and a slight lowering of each of the cellular company's antennas. A neighborhood organization was involved in the process and it appeared at a municipal counsel meeting to express its concern. It argued that the tower "would be unsightly and negatively impact property values and the character of the neighborhood." It also argued that the tower was not in conformity with the "Township's Telecommunications Ordinance."

According to the organization, at a minimum, that the cellular companies "were required to apply for zoning or planning variance approvals and, as private companies, they [were] not exempt from the municipal telecommunications ordinance although co-located on a municipal communications tower on property leased from [the municipality]." In response, the municipality asserted that the tower was "necessary for reliable and vital police, fire, emergency and municipal services and communications, particularly given the topographical variations in [the municipality]."

A 1955 New Jersey Supreme Court decision dealt with a question as to whether a municipality is exempt from a zoning regulation in acquiring property in a residential district for an administration building or assembly hall. That Court "found that the local zoning ordinance did not prevent the municipality from[exercising] its power to determine the location of municipal facilities."

Further, the local ordinance exempted from zoning regulations "any municipality owned, operated or controlled building, structure, facility or use, either existing or proposed." According to the Court, that language was broad and did not purport to limit municipal activities. The validity of the ordinance was not at issue. Nonetheless, the Court needed to assure itself that the municipality was not acting as "a private entrepreneur."

With those principles in mind, the Court held that the municipality could not be restrained from determining the location of a municipality-owned communication tower for police use, but the power to choose a location must be "reasonably exercised in response to the public need." In that regard, some of the "[c]onsiderations to be weighed include the overall zone plan as well as the impact on surrounding properties and evaluation of alternate sites." The extent of deviation from the zone plan is relevant. Searching for a "reasonable" alternative is important, but the reasonableness is actually to be "based on efforts by the municipality to comply with a zone plan." Consequently, the Court found that the municipality could "construct a communications tower at its police headquarters without obtaining zoning approvals, but its construction plan [must be] subject to review to determine whether the [municipality] acted reasonably in the exercise of its authority." The review could not be "in the nature of satisfying the positive and negative criteria for a use variance" because that would render "exemption from zoning regulation meaningless."

The Court analyzed the review process that had taken place in connection with the bidding and thought that the neighborhood association and others did not have the complete opportunity to raise objections. According to the Court, even though the municipality agreed, and in good faith attempted to address the neighborhood organization's concerns, the "discussions were abbreviated and informal meetings where experts were heard [did not leave a] public record for review preventing the Court from determining whether the municipality met the test of reasonableness." Consequently, it ordered that the municipality conduct further public hearings.

Editor's Comment: If the City can choose to zone and not to zone, why in the world should the court be justified in applying the level of scrutiny it did in reviewing the City's decision? It turned a general public policy question into what is, despite the Court's denials, effectively a variance proceeding.

Some may see the decision as Solomonic. To the editor, it's another example of judges abusing their legal review power to put themselves effectively in charge of determining all that's right and good. These weren't thugs or charlatans. They were elected City officials. The remedy for abuse, if any, should be political.

TELECOMMUNICATIONS; CELL TOWERS; ZONING: A private telecommunications company locating its cell tower on public land pursuant to an agreement with a public agency so that the tower, at least in part, serves a public interest, is exempt from zoning regulations if the agency's action itself is so exempt. ***Hills of Troy Neighborhood Association, Inc. v. Township of Parsippany-Troy Hills 392 N.J.Super. 593, 921 A.2d 1169 (Law Div. 2005) approved for publication April, 2007*** (discussed further on another item under the same heading)

The facts of this case are discussed in a separate item discussing whether the municipal agency itself is exempt from its own zoning laws in locating a privately owned telecommunications tower with collocation facilities for private internet services on municipally owned land. The court held that there was an exemption, but that the municipality had an obligation to make a reasonably determination of governmental need, subject to public participation.

As to the corollary issue as to whether the cellular companies, as private companies, shared any exemption, the Court realized that this was a question of first impression. Nonetheless, it felt that prior case law "and statutes provide[d] guidance in first viewing zoning regulations in terms of the use of land rather than the legal form that ownership or possessory interests may take." Consequently, it felt that "[i]n this regard, if the use is by the municipality engaged in government business for public purposes, and it is a reasonable exercise of its authority, its exemption from zoning regulation may extend to those who join in advancing that public purpose. Status as a public enterprise alone should not control even though the private enterprise receives financial or other private benefits." Here, the municipality "was replacing its headquarters and its communication tower for police, fire and other emergency services, a significant public purpose to be located on a major highway, . . . It sought to enter into an agreement with [two cellular companies] to construct a tower at no cost to the municipality and to obtain rent for the private antenna to be co-located on the tower. Further, the nature of the private enterprise itself [was] to enhance wireless communications which enhances the general welfare under The Telecommunications Act of 1996." Under those circumstances, the Court held that "the private telecommunication providers herein may share in the exemption from zoning regulations enjoyed by [the municipality] upon the reasonable exercise of its authority. The fact that the companies will receive a private benefit is secondary and outweighed here by the public interests served – a police headquarters and communications tower for emergency services."

TELECOMMUNICATIONS; MUNICIPAL SERVICES: City's requiring connection of all new construction to city's broadband telecommunications system is an unconstitutional taking. ***Home Builders Ass'n v. City of Lebanon, 854 N.E.2d 1097 (Ohio App. 12 Dist. 2006), appeal den'd 854 N.E. 2d 1097 (8/2/06),*** discussed under the heading: "Constitutional Law; Due Process; Takings; Regulatory Takings."

TRUSTS; BENEFICIARY CONTROLLED TRUSTS; BANKRUPTCY; HOMESTEAD: A Chapter 7 bankruptcy debtor may claim the homestead exemption where the real property was transferred to a revocable trust prior to the bankruptcy and the bankruptcy debtor was both the settlor and a beneficiary of the trust. ***Redmond v. Kester, 2007 WL 1649931 (June 8, 2007),*** discussed under the heading: "Homesteads; Transfer to Trust; Homestead Exemption; Title Insurance."

VENDOR/PURCHASER; CONDITIONS; FINANCING: A potential homebuyer does not violate the terms of the purchase and sale agreement by engaging in a parallel transaction on a second home where mortgagee, in preapproval process before contract with seller, had indicated buyer likely would qualify for a loan notwithstanding acquisition of the second home. ***Alfeo v. Dinsmore, 861 N.E.2d 491 (Mass. App. Ct. 2007).***

In November 2002, Gina Alfeo ("Alfeo") entered into a purchase and sale agreement (the "Agreement") to purchase a residential home from Mark T. Dinsmore and another owner (together, the "Sellers"). The Agreement contained a standard form of mortgage contingency allowing Alfeo out of the contract if a conventional bank or other institutional mortgage loan could not be obtained at prevailing rates, terms, and conditions. The Agreement was extended several times to allow Alfeo additional time to obtain a commitment, but Alfeo was eventually denied a loan and subsequently terminated the Agreement.

The Sellers refused to return the deposit, Alfeo brought suit for declaratory judgment, and the Sellers counterclaimed for breach of contract.

The Sellers' first claim stemmed from the source of Alfeo's rejection by the lender. While engaging in the above transaction, Alfeo also entered into a purchase and sale agreement on a second home and obtained a loan for that purchase and closed that transaction. Alfeo intended to live in the second home while remodeling the Sellers' home.

The Sellers claimed this second transaction constituted either fraud or a breach of good faith and fair dealing under their contract. The Sellers also claimed that Alfeo's mortgage application did not satisfy the requirements of the Agreement because it was made to a mortgage broker engaged in "table lending", meaning immediate resale at closing to a participating mortgage servicer, and thus was not made to either a conventional bank or an institutional mortgage lender. The trial court granted summary judgment for Alfeo, dismissing Sellers' claims and ordering a return of the deposit.

On appeal by the Sellers, the court of appeals (the "Court") first disposed of the issue of the mortgage broker's status. Citing its status as a licensed mortgage broker and mortgage lender in the state of Massachusetts, and also its status as an approved Federal Housing Administration lender, the Court found that a mortgage broker engaging in immediate resale is still an institutional mortgage lender. The Court also noted that determinations by such brokers are governed by industry standards and that even large underwriting lenders use funds from outside sources. The Court then addressed Alfeo's parallel transaction.

The Court found that because Alfeo had obtained a preapproval for a second home, and because the mortgage broker had indicated approval was likely, the Sellers could not make a showing of bad faith, even though the second transaction was not disclosed to the Sellers. On the facts, the Court agreed with the trial court's finding that there was no affirmative duty to disclose that information. The summary judgment of the trial court was affirmed in all respects.

VENDOR/PURCHASER; INSTALLMENT LAND CONTRACTS; EQUITABLE MORTGAGE; TRANSFER IN LIEU OF FORECLOSURE: Although Indiana typically will require a seller to foreclose an installment land contract as an equitable mortgage rather than to utilize the contract forfeiture remedy, where buyer willingly foregoes his equity interest in property by conveying such property back to seller per the forfeiture clause of a land sale contract, buyer will not be entitled to compel seller to foreclosure on such property. ***Armstrong v. Keene, 861 N.E.2d 1198 (Ind. App. 2007).***

Seller and Buyer entered into a Conditional Contract for Sale of Real Estate for the sale of a restaurant. The purchase price was $100,000 with a down payment of $20,000 and monthly payments of $811.42 for a period of 9 years.

The Contract provided that Buyer was responsible for real estate taxes and insurance on the property and also contained the following forfeiture terms: if Buyer failed to make any payment under the Contract for a period of 30 days beyond its due date, the Contract would become null and void and Buyer would be required to surrender and deliver the real estate back to Seller.

Seller and Buyer also entered into a contract for the sale of the inventory, equipment, stock and trade, and retail liquor license of the restaurant. In December 1997, seven years into the term of the agreement, Buyer failed to make the monthly payment and failed to pay the real estate taxes. Buyer remained in possession of the restaurant and continued to operate it until March 1998, at which point Buyer executed a Bill of Sale where he granted, sold, transferred, and delivered to Seller for good and valuable consideration his interest in the restaurant.

On June 20, 2001, Buyer filed a Complaint for Breach of Contracts against Seller alleging that Seller had orally agreed to pay him $25,000 for the restaurant and $1140 for the inventory in exchange for Buyer transferring his interest back to Seller, but failed to pay him. Buyer also alleged that he was entitled to foreclosure of the real estate. Both parties filed motions for summary judgment, and the trial court held that the alleged oral agreement between the parties was unenforceable and that Buyer had voluntarily relinquished his equity interest in the property. Buyer appealed.

Buyer argued that the trial court erred in finding that he was not entitled to demand a foreclosure of the real estate based on *Skendzel v. Marshall*, 261 Ind. 226, 301 N.E.2d 641 (1973). In *Skendzel*, the Indiana Supreme Court considered whether to apply a forfeiture provision in a land contract or to entitle buyer to foreclosure on the real estate. That court observed that forfeitures are generally disfavored because a significant injustice results where the buyer has a substantial interest in the property.

The Court of Appeals in this case, however, found that the forfeiture clause was not at issue since Buyer had, upon defaulting, executed a Bill of Sale granting his interest in the real estate to Seller, thereby indicating a willingness to forego his equity in the restaurant. As a result, Buyer was barred from seeking foreclosure of the real estate. The Court of Appeals affirmed the trial court's grant of summary judgment in favor of the Seller.

VENDOR/PURCHASER; LAND DESCRIPTIONS: Contract sufficiently described the portion of vendor's land to be sold such that it didn't violate the Statute of Frauds where it states that parties have agreed upon boundaries and later survey will provide exact description. ***Schuler v. Graf, 862 N.E.2d 709 (Ind. App. 2007)***.

Schuler and Graf entered into a land contract that described "two surveyed parcels [one being approximately 5 acres and the other 6]. The exact acreage to be determined by survey….The boundaries of the two parcels have been agreed upon by the parties. . . . [U]pon completion of the survey the two legal descriptions shall be attached to this contract."

Prior to signing the contract, Schuler and Graf walked the property and discussed the proposed boundaries, marking some boundaries as they went. After the contract was signed, but before the survey was completed, Schuler asserted that the contract did not contain a legal description of the property and that no meeting of the minds existed.

The completed survey indicated that Parcel B was 7.64 acres, not the 6 acres put to writing in the contract. Schuler refused to sign any more paperwork, indicating that she did not wish to sell the land.

The Grafs filed a lawsuit and a *lis pendens* notice, and Schuler put forth the affirmative defenses of failure to satisfy the Statute of Frauds, absence of a meeting of the minds, and unenforceable contract.

The land was surveyed again, and the eastern boundary of Parcel B was adjusted to reflect Schuler's understanding of the boundary, shrinking the size from 7.64 acres to 6.896 acres.

During a bench trial, both Schuler and Graf testified to their understandings of the boundaries of the land to be sold based upon their walk and conversation. Schuler testified that she had agreed to sell the Grafs some property, but disputed one boundary established by the survey and Graf's testimony. The trial court ruled that there was a meeting of the minds on the description of the land, the boundaries had been agreed upon by both parties, and the contract should be honored. Schuler appealed.

The court of appeals wrote that to comply with the Statute of Frauds, a contract for the sale of land must: 1) be signed by the party against whom the action is being taken, 2) describe each party and the land with reasonable certainty, and 3) state the terms and conditions of promises made with reasonable certainty. The writing must also contain all terms without resorting to the parol evidence rule. The court stated that terms could be abstract or general, as long as they could be applied to identify the parcel "to the exclusion of all other property." Here, the court held that the contract in question adequately provided a means of identifying the property. Although the contract only described the land to be sold in terms of acreage, it did provide that "the boundaries of the two parcels have been agreed upon by the parties," indicating the existence of an understanding between Schuler and Graf. Testimony confirmed that the two parties walked the land together and agreed upon boundaries using landmarks, monuments, and adjacent boundaries. The description of the land in the contract signed by both parties was sufficient to meet the requirements of the statute of frauds. The court then held that the parties entered into a contract for the sale of real estate and a meeting of the minds occurred. Accordingly, the court of appeals affirmed.

Editor's Comment: The editor admits to being perplexed. If the rule is that the contract must contain an description of the property ascertainable without parole evidence, then how can the evidence of the parties' placing boundaries on the property be admitted? There was no reference to such activity in the contract. And without the monumentation, it would appear that there is no evidence of agreement on the boundary except in the parties' minds.

If this is a valid description, then what is left of the requirement for a writing? Surely it would be possible in every case to argue that the parties knew what they agreed, but just didn't put it into a writing. Normally this would not satisfy the Statute.

VENDOR/PURCHASER; SELLER'S REMEDIES; RESCISSION: Where compensation paid to seller is clearly inadequate, and there is some evidence of diminished capacity, court may rescind contract for unilateral mistake or basic inequity. ***Landers v. Sgouros, 2007 Westlaw 1575879 (Mo. App. 6/7/07***), discussed under the heading: "Deeds; Validity; Mistake."

VENDOR/PURCHASER; SPECIFIC PERFORMANCE; ATTORNEY'S FEES: A court may not permit a successful buyer in a specific performance action to credit the attorney's fee award against the buyer's obligation to pay the purchase price. ***Behniwal v. Mix 147 CA4th 621, 54 CR3d 427 (2007)***

The Behniwals finally prevailed in their action to compel the Mixes to honor their contract to sell their condominium unit to them for $540,000 and, in addition, were awarded over $250,000 in attorney fees. (The matter had gone to the court of appeal on at least three prior occasions.) The trial court ordered the attorney fees to be deducted from the purchase price, but that order was reversed on this appeal.

According to Justice Sills, who had authored all of the opinions in this interesting saga, the attorney fees award ranks below the deeds of trust on the seller's property as well as the seller's homestead declaration. The consequence of the ruling, as all apparently agreed, was that the Behniwals were unlikely to recover the attorney's fee claim. There were three deed of trust liens against the property – all imposed on the property after the litigation commenced. One was to a savings and loan association, and two were in favor of their attorney in this litigation. In addition, the court noted, the seller were entitled to a $150,000 homestead exemption. All added up, the only available equity for the buyers to reach, if their only right was to collect the attorney's fee award as a judgment, was around $90,000. But this does not take into account accrued interest that surely applied to the deeds of trust to the attorney.

On the other hand, stated Justice Sills, if the attorney fees were taken off the top, it would play "absolute havoc with the law of liens and lien priorities." 146 CA4th at 632.

Justice Sills reached this conclusion by some very elegant reasoning. He first determined that an attorney fees award in a specific performance action by itself does not reduce the price in the same way that an equitable adjustment might. (The older cases that seemed to say that were doing so only as a kind of "rough justice" in contexts where priority did not matter.) The fee award is not mere incidental relief to a specific performance decree, but rather an additional right-created by the attorney fees clause in the contract-with no special claim to any lien superpriority. Attorney fees are just a money judgment that will function like a lien (with concomitant lien priority) only after it has been recorded.

Reporter's Comment1: I had always innocently believed that a purchaser who was successful in a specific performance action, and who had an attorney fees clause in his contract, could deduct what he was awarded by the court for those fees from the amount that he would have to pay. Now I have learned that the rule is otherwise, but I have to say that I regret that and I would like to find some way to get around it.

First, let's talk about priority of the fee claim vs. liens that were on the property at the time that the specific performance began. In fact, in the end, either result pretty much gets us to the same conclusion.

It is hard to disagree with any of the court's reasoning, but the legislature may have superseded it by its treatment of offsets. The statement in CCP §431.70 that cross demands "are compensated so far as they equal each other" does not seem to make an offset depend on any particular priority status. If the Behniwals' attorney fees are treated as though they had already been paid to Mix (see *Murphy v FDIC* 38 F3d 1490 (9th Cir 1994)), any lien inferiority on their part would not matter because the cross demands were "deemed compensated." See *Murchison v Murchison*219 CA2d 600, 33 CR 285 (1963).

In fact, the judicial principle that offset is more appropriate when the cross party may be insolvent (and thus less likely to be able to honor its half of the burden; see *Erlich v Superior Court* 63 C2d 551, 47 CR 473 (1965)) seems also to run contrary to the notion that offsets are controlled by lien priority principles. In those cases, giving a litigant an offset right certainly worsens the position of its adversary's other creditors.

Nor would offset necessarily wreck our system of priorities, as Justice Sills seems to fear. No preexisting deed of trust on the seller's property would be pushed down by a buyer's offset because a third party lender, not being a party to the specific performance litigation, would find its instrument unaffected by it – only the identity of the trustor would change. The successful purchaser would take title to the property, subject to whatever balance there was on existing deeds of trust, and no attorney fees award would trump those liens. If the balance of cash the purchaser then pays isn't enough to retire the preexisting liens entirely, they just stay on the title. Sooner or later, the purchaser will have to pay them off.

Reporter's Comment 2: But what about the priority of the fee award against later claims?

In *Behniwal*, the lien priority that had to be dealt with concerned three interests that were created after the purchasers had filed their lawsuit and recorded their *lis pendens*. Even if the right of offset was subject to the rules of priority, why did the attorney fees award have to go behind those three later claims?

Justice Sills's answer was that, as a technical matter, the attorney fees could achieve lien status only after a money judgment had been rendered and recorded, all of which happened after the other three interests went of record. But that only triggered the question: Why shouldn't the purchasers' award relate back to the date they recorded their *lis pendens*, which was before those three interests appeared?

Relation back is what I would have expected, but in Justice Sills's view, the *lis pendens* only notifies third parties that the buyer is suing to enforce a sale of the land at the stated contract price (unreduced by offsets) (147 CA4th at 638):

"A buyer or moneylender, then, could have reasonably relied on the buyers' own pleadings to conclude that, should the buyers be successful, the court would force the sellers to convey the property for the contract price of $540,000. . . . [A] lender could also reasonably rely on the pleadings to conclude that the property could be safely encumbered up to that $540,000 amount."

That the pleadings also gave notice of a potential attorney fee award did not matter because that award would be only a later money judgment that could not relate back to the earlier *lis pendens*. Justice Sills treats the *lis pendens* differently than a recorded deed of trust, which puts all subsequent parties on notice that attorney fees in any foreclosure will also come off the top and before them.

That proposition is true only after this decision has made it a correct statement, but before the decision was announced, I believed that the general principle was that a *lis pendens* "Puts purchasers and encumbrancers on notice that they will take subject to any judgment thereafter entered in the case; " Will bind them to any judgment that might be entered (see *BGJ Assocs., LLC v Superior Court* 75 CA4th 952, 89 CR2d 693 (1999) ; *Ahmanson Bank & Trust Co. v Tepper* 269 CA2d 333, 74 CR 774 (1969)); and would apprise them of the possibility that an award of attorney fees could be offset against the purchase price.

Despite this opinion, I think attorneys should still caution subsequent takers as to this risk. There remains a real danger that they could be charged with inquiry notice of all plaintiff's claims, including attorney fees.

Priority Against the Other Claim I think doubts about priority would be even stronger for the law firm that took the second deed of trust. How can those lawyers claim to be BFPs without notice, entitled to protection of the recording acts against a plaintiff's attorney fees claim, when they are engaged in representing their client against that claim-and, therefore, surely have actual knowledge of it? We are not told the circumstances of that transaction in *Behniwal*, but if a law firm's deed of trust was given to secure payment for services to be rendered, would not those fees have the status of future advances made with actual knowledge of the junior claim? (I second the observation made by Justice Sills that the losing side's attorney is the only real winner in the case.)

Finally, I would have doubts about assuring the defendant sellers that any homestead they filed after they had been sued would protect them against their buyers. Generally, a later filed homestead can prevail against an earlier filed action, but in this case that earlier action sought attorney fees that the sellers had agreed to in their sales contract (executed before anything else had happened). I would worry that the attorney fees clause in the sales contract could justify treating the fee award as a kind of preexisting consensual claim against which the homestead might not prevail. (Miller & Starr say that the homestead exemption does not apply against an equitable mortgage, whether it is recorded or not. 5 California Real Estate §13:43 (3d ed 2000).)

But all of my speculations turn out to be faulty in light of the decision in *Behniwal*, which significantly raises the stakes for purchasers contemplating specific performance litigation. Not only must they be prepared to prove that their contract is just and reasonable (as well as merely enforceable) and be prepared to stay ready, willing, and able throughout the entire litigation to pay the purchase price whenever the vendors are ordered or offer to perform, but now they also must be prepared to have their expected award of attorney fees held subordinate to any liens the sellers (involuntarily or voluntarily) impose on the property during the litigation, devastating their ability to offset those fees against the price they will still have to pay.

Justice Sills is too respected, and has thought too hard about this case, to make it likely that any other appellate tribunal will disagree with him. The legislature is certainly not going to bother itself with the small (and difficult) problem this case presents. So I predict that this is going to stay as our rule.

Reporter's Comment 4: Is there a way for purchasers to reduce the risks this rule creates? I cannot offer much help if the deal has already fallen apart and they are about to sue. They will not receive a fee award until the end, and then it will rank only as a money judgment with no superpriority despite any lis pendens they have earlier filed. Maybe they could file an attachment enabling the judgment to relate back to the lis pendens filing, but can purchasers both attach and lis pendens the very property they are attempting to purchase? Even if they can, our supreme court has held that a later homestead prevails over a prior attachment anyway. *Becker v Lindsay* (1976) 16 C3d 188, 127 CR 348.

Better language in the agreement, inserted at the drafting stage, is the only hope. Thus, some provision in the contract should give lien status to any attorney fees later awarded and also provide for relation back to the date of contract execution. It would be hard, if not impossible, to negotiate any individualized version of that kind of arrangement, but published forms could do that for everybody.

Since attorney fees clauses occur in most contracts, and are therefore presumably desirable to both sides, a supplemental provision in the same paragraph that gives those fees some teeth might generate little controversy at the early contract formation stage. If the same provision also allowed the prevailing sellers to use their fee awards to include the purchasers' deposits (even when there is no, or only a lesser, liquidated damages clause), both sides might be better off.

The Reporter for this item was Professor Roger Bernhardt of the Golden Gate Law School, writing in the California CEB Real Property Reporter. Reprinted and edited with permission.

WASTE; LIFE TENANT; TIMBER: Life tenant may not cut timber except for firewood, and any further timber cutting is waste and actionable even if the value of the property is not thereby diminished. ***Landers v. Sgouros, 2007 Westlaw 1575879 (Mo. App. 6/7/07)***

Here the court set aside a deed from a life tenant to a purchaser due to mistake of fact. Before the deed had been challenged, however, the purchaser had sold timber rights and had received a payment of $3950 for the rights and for the first cutting of the timber. The plaintiffs were not the life tenant, but rather the holders of the remainder, who argued that they were entitled to damages for waste.

The defendants argued that there was no waste absent a showing that the value of the property had been reduced. The court disagreed. It quoted from a 100 year old Missouri case that gives an interesting insight into the issue:

"Waste is that which does a lasting damage to the freehold or inheritance, and tends to the permanent loss of the owner in fee, or to destroy or lessen the value of the inheritance. In this country, where (at least until recent years) timber in many places is a hindrance to the enjoyment of the estate, whether it be for life or in fee, the law is that cutting timber for the purpose of cultivation (if it did not lessen the value of the inheritance) is a privilege following a tenancy for life, when it was necessary for the proper and reasonable enjoyment of his estate, and as long as he only acts in so doing in conformity to good husbandry, regard being had to the situation of the country and the *comparative* value of the timber. But this is a privilege which can only be exercised for the purpose mentioned, *i.e.*, the proper enjoyment of the estate, which is hindered by the timber. So it has been held that the tenant cannot cut the timber merely for sale."

Inexplicably, however, the court cited one measure of damages and then awarded an entirely different measure with no statement of justification:

Appellants also assert that "[w]hile the [t]rial [c]ourt did not specifically designate the theory under which this decision was made, the case was tried based upon waste by a life tenant." As such, Appellants maintain there must be evidence as to the value of the Farm before the timber cutting and the value of the Farm after the timber cutting. We disagree. "In an action for waste, 'where the damage is small in comparison to the total value of the property and is readily ascertainable and where the verdict is not excessive, the amount of such damage may be arrived at by determining the cost necessary to restore the property to its former condition.'"

Fair enough. But the court then ordered that the entire $3950 received by the defendants be paid over. But this was not the cost of restoration. This was imply the gain enjoyed by plaintiff. How does this fit the waste measure?

Comment 1: The result is appropriate. The cost of restoring trees to a wild timbered lot would seem to be too high, and therefore the court just took the ill gotten gains enjoyed by the defendants and paid to the injured plaintiffs. But there is a problem in defining this as an appropriate measure of damages for waste.

Comment 2: One appropriate approach might have been to view this as an action in conversion. Another might have been to treat the case as one for equitable restitution. Either theory would have delivered the court to where it wanted to be.

WATERS AND WATER RIGHTS; STORM WATER RUNOFF: Storm water drainage can give rise to a prescriptive easement, but such an easement is limited in both location and scope to that occurring during the period over which the easement is acquired, and the reasonableness of a landowner's drainage onto neighbor's property must be assessed against the harm caused to adjacent property and the availability of remedial measures. ***Trenz v. Town of Norwell, 861 N.E.2d 777 (Mass. App. Ct. 2007)***, discussed under the heading: "Nuisance; Storm Water Runoff."

WORDS AND PHRASES; "GARAGE:" A garage is a structure where motor vehicles and household items are stored, and does not include a facility with second story living accommodations, even if the first floor also is used for such storage. ***Lussier v. Zoning Board of Appeals of Peabody, 854 N.E.2d 1236 (Mass. 2006).***

WORDS AND PHRASES; "RESIDENTIAL ONLY:" A restriction that property shall be used for "residential purposes" does not restrict the use of the property for daily and weekly rentals. ***Scott v. Walker, 2007 Westlaw 1651138 (Va. 6/8/07)***, discussed under the heading: "Servitudes; Restrictive Covenants; Use Restrictions; "Residential Only."

ZONING AND LAND USE; ESTOPPEL; VARIANCES: Landowner may invoke estoppel doctrine to obtain zoning benefits conferred in error where landowner has relied upon such benefits and where the error resulted from a plausible, albeit incorrect, reading of the zoning rules. ***Hartung v. Baker, 2006 Westlaw 1063291, Docket No. BER-L-1499-05 (N.J. Super. L. 4/21/06***) ***(unreported decision)***

Although an unpublished opinion, this is a really superb example of a winner in the elusive chase to invoke zoning estoppel, and is worth a read for anyone with a problem in this area.

In 1997 Hartungs purchased a home with a detached garage. The garage was five feet five inches from their neighbor's boundary – within the five foot sideyard setback requirement.

By 2004, the home was too cramped, and Hartungs elected to undertake a major remodel. The remodel would add a half story to the house and a wing that would extend to and incorporate the garage into the structure of the house. They submitted an informal inquiry to the city building department, with a chart indicating setback dimensions for their project. A diagram clearly indicated that the addition would result in the garage, now incorporated into the house, being five feet, five inches from the boundary, and the chart indicated that this satisfied the five foot sideyard setback. Hartungs did not take into account the fact that the zoning code had a ten foot sideyard setback for residences. The five foot setback was only for free standing ancillary structures.

The building department inspector also missed the significance of connecting the house to the garage, and certified the rough plans as approved. Hartungs then retained an architect and undertook a more formal design which they submitted to the same inspector for a building permit, and he again approved the plans and issued the permit. The appeals court noted that the inspector signed the architectural plans as "approved" less than six inches from the point on the plans that showed the five foot five inch side yard setback. Hartungs then set out to construct their project, and four months of construction commenced, during which the foundation works clearly showed that the completed project would be within five feet, five inches of the boundary.

Ultimately, a neighbor complained to the City and the building department issued a "stop work" order. In the dispute the affected neighbors filed a tax appeal, alleging that the proximity of the Hartungs' new residence to their property diminished the value of their property, entitled them to an adjustment in their appraised value. The city cited this tax appeal as evidence that it would be inequitable to permit Hartungs to continue on their unlawful course of construction, due to an error that the city characterized as "self created" by Hartungs.

The appeals court judge cited to *Jantausch v. Borough of Verona*, 41 N.J. Super. 89, 94 (Law Div. 1956), aff'd 24 N.J. 126 (1957), as the "polestar" decision in this area. *Jantausch* took the position that for an estoppel claim to lie, administrative officials must have made an "erroneous and debatable interpretation of the ordinance" in "good faith and within the ambit of [their] duty" upon which the owner relied in good faith. A subsequent New Jersey decision arguably amended the test by stating the approval agency's original decision must be based upon "an issue of construction of the zoning ordinance or statute, which, although ultimately not too debatable, yet was, when the permit was issued, sufficiently substantial to render doubtful a charge that the administrative official acted *without any reasonable basis* or that the owner proceeded without good faith."

The court characterized a successful zoning estoppel case as a kind of "holy grail" that many seek but few actual obtain. It provided a chronological list of all important New Jersey appellate decisions on the subject to demonstrate that a successful outcome for the landowner in these cases is indeed elusive. It then set forth nine factors that might be taken into account in the "totality of circumstances" analysis to establish whether estoppel is appropriate, assuming the preliminary requirement of *Jantausch* is satisfied:.

1. What is the size or scope of the deviation from the zoning ordinance?

2. What is the nature or quality of the deviation from the zoning ordinance?

3. What is the impact of the deviation from the zoning ordinance upon the immediate neighborhood?

4.What is the impact of the deviation from the zoning ordinance upon the overall zone plan and zoning ordinance?

5. What is the respective culpability of the parties?

6. What is the status of the party claiming the benefit of the equitable estoppel.

7. Is there evidence of collusion or the potential for collusion?

8. What is the hardship to the party claiming the benefit of equitable estoppel?

9. What is the detriment to the public interest if the estoppel is applied?

Despite the city's assertion that Hartungs misled the City building inspector, which led to the erroneous approval, the court held that the *Jantausch* test was satisfied here. It characterized estoppel as the "proud champion of justice, morality, and common fairness." (Put that in your "useful quote" file.)

Comment: The case is a real "keeper," but unfortunately states a relatively narrow basis for estoppel. It is sensible, however. If the city official's error is patent, it is up to the landowner to identify the error and inappropriate to rely on it. But it this the only situation in which other jurisdictions will grant an estoppel?

Compare: The following cases are all prior DD's.

Congregation Etz Chaim v. City of Los Angeles, 371 F. 3d 1122 (9th Cir. 2004) (City will be estopped from reneging on building permit after applicant has invested substantially in project, even when permit issued erroneously and in violation of settlement agreement that applicant previously had entered into with City*)* *(*the editor thought this case to be clearly wrong); *Bonaventure International, Inc. v. Borough of Spring Lake*, 350 N.J. Super. 420, 795 A.2d 895 (App. Div. 2002) *(*When a municipality is aware of long-established but unlawful use and implicitly approves it by referring to it as apparently lawful in public documents, the municipality is equitably estopped from challenging the expanded use as against a good faith purchaser of the property*); Equicor Dev. v. Westfield-Washington Tp.,* 758 N.E.2d 34 (Ind. 2001) (Zoning commission is subject to the doctrine of equitable estoppel when it fails to point out a formal deficiency in a plat and an applicant reasonably relies on the commission's silence);. *Pingitore v. Town of Cave Creek*, 981 P.2d 129 (Ariz. App. 1998). (Town government may be estopped from enforcing zoning ordinance that conflicted with construction plan where town officials had approved significant elements of proposed project based upon compliance with earlier ordinance.) *But see: Ogar v. City of Haines*, 51 P.3d 333 (Alaska 2002) Issuance of building permit for a part of landowner's project does not constitute an "assertion of a position" with respect to other aspects of the project sufficient to invoke equitable estoppel permitting the project to proceed.

ZONING AND LAND USE; PROCEDURE; STANDING: The Massachusetts statute barring unregistered foreign limited liability companies transacting business in the Commonwealth ("LLC"s) from bringing suit in state courts does not apply to administrative proceedings. ***Cottone v. Cedar Lake, LLC, 854 N.E.2d 456 (Mass.App.Ct. 2006)***.

Cottones obtained a building permit to erect a garage and attached deck on their property. After the improvements had been erected, Cedar Lake, LLC ("Cedar Lake"), the owner of an abutting lot, hired a surveyor, who determined that the Cottone's garage was located about four feet from the property line and that the deck encroached on Cedar Lake's property. Cedar Lake then filed a complaint with the building inspector, requesting enforcement of the fifteen-foot set-back mandated by the applicable zoning by-law.

The building inspector denied Cedar Lake's request for relief, and Cedar Lake filed an appeal to the seven-member zoning board of appeals (the "Board") which granted Cedar Lake's request for relief by a vote of five to two.

Cottones then brought an action in the trial court, challenging Cedar Lake's standing before the Board as well as the authority of the Board to grant Cedar Lake's request. The trial court granted Cedar Lake's motion to dismiss, and Cottones appealed. The Court of Appeals affirmed. As Cottones had removed the deck in question prior to commencement of the action, the issues before the Court pertained only to the set-back requirement with respect to the garage.

The first matter at issue was Cedar Lake's standing to appeal the decision of the building inspector to the Board. Cedar Lake was a Connecticut LLC which had failed to comply with the Massachusetts statutory requirement that foreign LLCs transacting business in the Commonwealth register with the Secretary of State. In arguing that Cedar Lake lacked standing before the Board, Cottones cited M.G.L. c. 156C, §54, under which an unregistered foreign LLC transacting business in the Commonwealth is barred from bringing an action or seeking recovery in the state's courts.

The Court rejected the argument that this statute barred Cedar Lake's appeal to the Board, finding no support in the unambiguous language of that statue for Cottones' contention that it applies to administrative proceedings as well as judicial proceedings.

Cottones then argued that Cedar Lake did not qualify as a "person aggrieved" within the meaning of M.G.L. c. 40A, §8, the statutory provision governing Cedar Lake's appeal to the Board. In support of this argument, Cottone cited *Save the Bay, Inc. v. Department of Pub. Util*, 366 Mass. 667 (1975), which it read to mean that standing under the M.G.L. c. 40A §8 extends only to those who would have standing in a court of law. The Court rejected this broad reading of *Save the Bay*, concluding that "standing at the zoning board of appeals level is limited solely to an analysis of whether the party has a specific and substantial interest, such that they are a 'person aggrieved.'" *Cottone* at 459. Having asserted "a plausible claim of a definite violation of a private right, a private property interest, or a private legal interest," Cedar Lake satisfied the requirements for standing before the Board. *Id.* at 854, (quoting *Harvard Square Defense Fund, Inc. v. Planning Bd. Of Cambridge*, 27 Mass.App.Ct. at 492-493, 540 N.E. 2d 182).

The Court declined to decide whether Cedar Lake would have had standing to appeal an adverse ruling by the Board, noting however that it was not barred from defending itself in the present action brought by Cottones.

Finally, the court rejected the argument that the Board acted outside the scope of its authority by mandating that Cottones take one of several specified actions within sixty days of its decision, finding that Cottones were required only to submit a plan for compliance by the specified date and further that any requirement to demolish non-compliant structure would been within the Board's authority anyway.

ZONING AND LAND USE; PUBLIC USES: A municipality that selects a telecommunications tower site for governmental use need only act reasonably in its site selection and, if its zoning ordinance exempts its sites from the need to obtain land use approval, it need not obtain such, even if its tower will be shared by private cellular service providers. ***Hills of Troy Neighborhood Association, Inc. v. Township of Parsippany-Troy Hills 392 N.J.Super. 593, 921 A.2d 1169, 2005 WL 3050995 (Law Div. 2005) , approved for publication April, 2007.***, discussed under the heading: "Telecommunications; Cell Towers; Zoning."

ZONING AND LAND USE; RELIGIOUS ACTIVITIES: Church did not have a vested right to continue operations in violation of a zoning ordinance. ***City of Elgin v. All Nations Worship Center, 860 N.E.2d 853 (Ill. App. Ct. 2006)***.

All Nations Worship Center ("All Nations") began conducting worship services in business district zoned AB, in which churches were not allowed as either a permitted or a conditional use. All Nations applied for a planned unit development permit, which was denied, with the City of Elgin ("City"). The City then filed a complaint alleging that All Nations was in violation of the zoning ordinance.

All Nations counterclaimed that the ordinance violated the Equal Protection Clause and the Religious Land Use and Institutionalized Persons Act of 2000 ("RLUIPA") because the AB zoning allowed for various types of nonreligious assemblies, but not churches. The City then amended its zoning ordinance, allowing All Nations to apply for a conditional use permit. The City withdrew its original complaint, and the trial court dismissed All Nations' counterclaim.

All Nations asserted that prior to the City's change in zoning, it acquired a vested right, allowing it to continue its operation without a conditional use permit. All Nations asserted that the original zoning ordinance was unconstitutional and therefore void *ab initio* (invalid from the outset). Contending the ordinance never legally existed, All Nations claimed a vested right under the law in existence before the original ordinance.

The Appellate Court held that there were two flaws to the All Nations claim. First, the void *ab initio* doctrine applies only to statutes or ordinances that are invalid on their face, not as applied. All Nations' claim was against the ordinance as applied.

Second, a party acquires vested rights by treating an ordinance as purportedly valid and attempting to comply with it as written. Here, All Nations proceeded to conduct worship services in violation of the ordinance as written, deeming it to be unconstitutional. The court wrote that a party is not empowered to determine for itself whether an ordinance is unconstitutional. All Nations did not acquire a vested right by violating a valid ordinance. The Appellate Court affirmed the judgment of the circuit court, dismissing All Nations' claim.

ZONING AND LAND USE; SPOT ZONING: A rezoning from light industrial use to a flood prone conservancy zone was not irrational "spot zoning" where evidence of flooding had been presented, and ulterior motives are irrelevant to any such analysis. ***Andrews v. Town of Amherst, 862 N.E.2d 65 (Mass.App.Ct. 2007).***

In the Land Court's ruling in favor of plaintiff, the judge agreed with plaintiff that the action of the Town of Amherst (the "Town") in rezoning a large portion of plaintiff's land from light industrial to flood prone conservancy ("FPC") constituted illegal "reverse spot zoning." The rezoning was the result of a citizen's petition, which was presented to the Town along with documentary and technical evidence that the subject parcel should be included in the FPC.

In general, a municipality is given broad authority and deference in regulating land use and zoning under the Home Rule Amendment of the Massachusetts Constitution, only limited by whether the local enactments violate state law or other constitutional provisions.

So-called "spot zoning" would constitute such a violation as a denial of equal protection, that is, not treating owners of like parcels of land alike, under the state and federal constitutions. To counter such a claim, the zoning enactment must fall within the broad police powers of the town to promote the health, safety and welfare of its citizenry.

To this end, Massachusetts case law supports the notion that so long as the town's action is otherwise justified based on these powers, any actual or ulterior reason for such action is irrelevant. As the challenging party, the plaintiff had the heavy burden of showing that the rezoning action here conflicts with the enabling act which established the FPC. The appellate court noted that if the reasonableness of the zoning action is even "fairly debatable," it would be upheld.

The court then launched into a fact-specific inquiry as to the situation of the parcel in question and the use and zoning of neighboring parcels. While the amendment changing the FPC line in the plaintiff's parcel did not include such a change in neighboring parcels, the court felt that those parcels were already under zoning and use restrictions that were similarly restrictive in nature, and thus a widespread rezoning was unnecessary to address the Town's concern in protecting farmland against flooding. The court declined the opportunity to second-guess the town as to extent of predicted flooding and the need to revise the FPC line, and noted that availability by other means of regulating building on flood-prone land does not invalidate the Town's action. Furthermore, even if plaintiff demonstrated that the Town relied on false or problematic data, the court held that it would still not set such a vote aside. The enactment of the zoning amendment was thus held a constitutional and valid exercise of the Town's police powers, and the decision of the Land Court was reversed.

ZONING AND LAND USE; VARIANCES; INTERPRETATION: A variance for the construction of a garage extending beyond setback restrictions is limited to the construction of a structure for storage only, and cannot be relied upon to construct a structure providing living space, even where the "footprint" might be the same. ***Lussier v. Zoning Board of Appeals of Peabody, 854 N.E.2d 1236 (Mass. 2006).***

Lussier purchased a home in 1996. The seller had obtained a variance for the home in 1995 (the "1995 variance") to construct a one-story, two-car garage that, though otherwise zoning compliant, maintained only a one foot setback rather than the required twenty feet. After purchasing the property, Lussier constructed the garage.

In 2003, Lussier sought and received a building permit and began construction on a second story of the garage, that would exceed the footprint, to be used as living space. Sheehans own the abutting property burdened by the decreased setback. Sheehans made a demand on the building inspector for an enforcement action, and when refused, appealed to the zoning board of appeals of Peabody. The Board granted the Sheehan's request on two grounds: (i) violation of the zoning ordinance's setback requirement and (ii) violation of the 1995 variance.

The Board found that the addition required a new variance or modification of the 1995 variance, and overturned the building inspector's refusal for an enforcement action. Lussier appealed.

The Superior Court entered summary judgment for Lussier with no explanation. The Board and the Sheehans appealed.

The Supreme Judicial Court, after transferring the case from the Appeals Court, found that variances, which are subject to limits of time, use and structure, are to be sparingly granted. Therefore, the words of the variance are to be construed against the individual and in favor of a board.

The Supreme Judicial Court looked to language of the variance, a garage with stated dimensions. While the term "garage" is not defined in the zoning ordinance, it does have a common understanding and usage as being where motor vehicles and household items are stored.. Because the use of a garage is for such storage activities, it is significantly less disruptive and intrusive than living space. Therefore, the court found that the word garage must be read from the variance to not include living space.

Finally, there were plans filed with the initial variance application, but not incorporated into the variance decision. Apparently these plans would have shown the full scope of the "garage" project, including the second story and the proposed dimensions. The court explained that while plans would have been helpful in determining scope, they cannot be relied upon without such reference in the decision.

Comment: Note that although the issue of the increased footprint might have decided the case, the court elected to reach further and to define variances including "garages" and to limit such variances to structures that fit that use.

In light of the many and varied uses of garages in modern times, it is interesting that the court felt it necessary to make such a leap. It is not uncommon, for instance, for hobbyists to use garages as workshops. They might use electric saws or other equipment that would cause considerably greater impact on neighbors than residential uses. Is such use somehow precluded by the terms of a variance? What about the general zoning law permitting, for instance, free standing "garages?" The editor sees the beginnings of a slippery slope here.