ABA Real Estate Quarterly Report

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Sponsor:
Section of Real Property,
Trust & Estate Law
American Bar Association

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Quarterly Report on Current Developments in Real Estate Law

October 1, 2007 to December 31, 2007

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ABA Section on Real Property, Trust and Estate Law
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Statement of Editorial Policy:

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

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

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

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

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ADVERSE POSSESSION; PUBLIC PROPERTY: Real property owned by a park district established under a statutory scheme cannot be acquired by adverse possession, even when the park district acquires the title only two years before running of the claimant's 21 year adverse possession period. ***Houck v. Board of Park Commissioners of the Huron County Park District, 876 N.E.2d 1210 (Ohio 2007).***

The case is of some interest because it involves a conversion of abandoned railroad property to a "rails to trails" project. A park district acquired the right of way for trail purposes only two years before claimant's adverse possession would have run.

On appeal to the Supreme Court of Ohio, appellants argued that Ohio's waiver of sovereign immunity trumps the general rule that adverse possession cannot be invoked against the state and its political subdivisions, thus making park districts amenable to suit. Appellants further argued that an earlier case, *Brown v. Monroeville Local School Dist. Bd. Of Ed.*, N.E.2d 767 (Ohio 1969), which held that adverse possession could be invoked against a school district, established a precedent that a park district is amenable to suit in adverse possession.

The Court first determined that because of its foundation in tort liability, the common law waiver of immunity was irrelevant for purposes of determining whether adverse possession may be invoked against a park district. The Court then distinguished *Brown* by noting that since the case was decided, at least half of Ohio's appellate districts had held that adverse possession cannot be applied against the state or its political subdivisions. The Court held that the general policy underpinning *Brown*, that political subdivisions of the state are not subject to loss of their streets or highways, supports the general rule that adverse possession does not apply against park-district property. Adverse possession of roads, streets, or highways is not permitted because it interferes with public use of the property in question. Similarly, allowing a park district to be adversely possessed would interfere with the public's enjoyment of park property.

The Court then stated that because of its great amount of property and relative lack of resources, a government entity should not be expected to monitor its land for trespassers with the same degree of vigilance as that of a private property owner, and that the public should not suffer for the government's negligence. Finally, the Court stated that adverse possession has long been disfavored, especially in cases such as this where the public would be deprived of enjoyment of public lands. Thus, the Court held that property owned by a park district established pursuant to R.C. Chapter 1545 is not subject to adverse possession.

A dissenting opinion argued that public policy does not require that a park district be permitted to hold title to land for an indefinite time with the vague intention of improving it at a future point, and that inspecting the property once every 21 years is not too great a burden even for an under-resourced park district.

ASSOCIATIONS; ASSESSMENTS; COLLECTION: A developer may not raise the annual maintenance charge set forth as a servitude in the master deed if the master deed limits such increases; but, if overall development and use scheme cannot be realized by fees set forth in master deed, and public policy demands, a court may modify the servitude to provide for increases. ***Citizens Voices Association v. Collings Lakes Civic Association, 396 N.J. Super. 432, 934 A.2d 669 (App. Div. 2007)***.

A development of about 1,100 homes was governed by master deeds that imposed certain covenants and restrictions on all of the parcels that made up the community. Most of the lots in the community enjoyed express easements for four lakes created and maintained by four dams and there were associated rivers, beaches, boat launches, playgrounds and parking facilities. All these facilities were owned by the original developer at the outset, and later were transferred to the Civic Association which, incidentally was not an owner's association consisting of all lot members. The provisions of the master deeds imposed a $48 annual maintenance fee on certain lots in the development, to be a lien against the properties. This fee was to be used to pay for the annual clean up and maintenance of all the recreational areas and surrounding woods. A separate agreement, that the court viewed as part of the scheme, imposed a cap of $48 on the amount of the assessment. In 1984 litigation, the Civic Association had been given the power to collect these assessments and the duty to perform the maintenance of the amenities. The Civic Association did collect continuously some fees and conduct some maintenance thereafter, although it appears that it did not collect all fees nor conduct all maintenance.

In 2000, the New Jersey environmental protection agency began correspondence with the Association that resulted in demands that improvements be made to the lakes and dams under the Safe Dams Act. The Civic Association determined that it couldn't meet the state demands with available assessment revenue, and thus amended the governing bylaws to increase the maintenance fee from $48 to $75 a year based upon anticipated environmental costs.

Encumbered property owners in the development sued the successor to remove the deed restrictions that imposed the maintenance fees for the recreational areas. The successor developer sought a declaratory judgment that the deed restrictions were valid and that it had the right to assess the property owners for additional costs for repairs, maintenance, and attorney fees. The Chancery Division found that the $48 charge was valid and enforceable as to those property owners subject to the deed restriction, but that the Association did not have the right to increase fees beyond the $48 annual charge in the deed restriction or to collect attorney fees, as the relevant documents did not permit increases but for any court rule or statute.

On appeal, the Appellate Division stated that none of the alleged failure to maintain property or collect assessments evidenced abandonment of a neighborhood scheme, and that the deeds made clear that encumbered property owners were to be charged $48 yearly by the developer for use of the community's lakes, beaches, parking areas, and recreational facilities. Accordingly, it affirmed the lower court's ruling, though it stated that a lower court retained the power to modify the covenants should a material change in circumstances occur. The court distinguished other cases that imposed upon parties benefitted by a common easement the right and duty to conduct maintenance on the easement facilities. See, e.g. *Lake Lookover Property Owner's Association v. Olsen* 2002 WL 220898 (N.J. Super. App. Div. 2/14/02) (The DIRT DD for 3/4/02) (Once a property owner begins to enjoy the benefit of an easement, it can not abandon the easement just to avoid a shared responsibility to pay the cost of maintaining it.) Here, the court ruled, and express agreement provided otherwise.

But the court went on to say that the decision here was not *res judicata* as to future attempts to increase the assessment should the current assessment indeed prove inadequate to fund the required maintenance. The record here didn't show that such additional funds would be needed if the assessments were collected diligently.

Indeed the real news of the decision is the court's further discussion of the hypothetical future case.

". . . Subsequent to our decision, there may well be a substantial capital improvement needed to preserve the purpose of the servitude. The cost of such improvements may be firmly identified and potentially even assessed against all of the owners by the DEP under the Safe Dam Act. N.J.S.A. 58:4-1 to -10. The lack of funds to maintain the lakes may well create a "blighted area" with a significant decrease in some or all of the property values in Collings Lakes. The health and safety of the public may be at issue if certain developments occur. There may be an unfair shifting of the burden to correct the problems with the lakes to the general public and individual taxpayers outside of the Collings Lakes community, which may require court intervention. Likewise, CLCA may fail to maintain the recreational areas and decide to abandon them. The lakes may be drained voluntarily by CLCA or by the DEP. The costs of maintaining the lakes may become prohibitively high for any group to undertake.

In such circumstances, we note a court has a reservoir of equitable power to modify or terminate a servitude should changes occur in the future which would make it impossible as a practical matter to accomplish the purpose for which the easement was created. See Restatement (Third) Property: Servitudes, supra, § 7.10(1) ("When a change has taken place since the creation of a servitude that makes it impossible as a practicable matter to accomplish the purpose for which the servitude was created, a court may modify the servitude to permit the purpose to be accomplished. If modification is not practicable, or would not be effective, a court may terminate the servitude.") Comment a to section 7.10 points out that the changed-conditions doctrine may permit a court to modify a covenant. Restatement (Third) Property: Servitudes, supra, § 7.10 comment a. It notes the doctrine may be grounded in the implied intent of the parties and public policy. Courts apply the changed-conditions doctrine with caution, though. Further, "[t]he test is stringent: relief is granted only if the purpose of the servitude can no longer be accomplished." Generally, covenants will be enforced in equity only so long as they remain reasonable in light of their purpose. See Id. § 8.3 comment e.

Therefore, if there were a material change in circumstances, pursuant to law, a court could modify the covenants restricting increasing the annual $48 charge, provided the modification was equitable as to all parties and would preserve the purpose of the servitude. Likewise, a court in the appropriate circumstance could determine modification is not practicable and terminate the easement and restrictions."

Comment 1: The editor has long maintained that the established common law doctrine imposing on beneficiaries of easements the responsibilities to pay for maintenance of the easement areas can resolve many of these alleged servitudes cases without making new law. To a certain extent, the court does that here, but then it gets into some rather far reaching discussion of modification of servitudes to carry out public policy that seems to be an invitation to totalitarian judicial rule over homes associations. This makes the editor very uncomfortable, despite platitudes that the test justifying the application of such draconian consequences is "stringent." The same court that chooses to take over the association is the court that decides whether the "stringent" test is met.

The editor believes that there are contracts, and there are politics, and the two are not the same. Here, the express covenant gave the association the power to look after the parks, playgrounds, and boat launches. It said nothing about the lakes and dams themselves. The beneficiaries of the easements in those facilities agreed to limit their cost exposure to $48 per year. So far as the editor is concerned, that's where it should stay. If the parties need more money to maintain those facilities, let them get together on the question. It's not the court's concern.

Comment 2: As to the maintenance of the dams and lakes themselves, there simply was not agreement by the parties. As the statute gives the state the power to impose maintenance costs on the "owners" of such facilities, which one would assume would include the owners of the easement rights in them, there is statutory authority to spread the costs among all such beneficiaries *unencumbered by the $48 limit, as the $48 limit pertained to an entirely different maintenance obligation.* The imposition of the cost of maintenance of the dams is indeed a public policy question, but it is not necessary to apply public policy through the device of the covenant scheme here. It is separately authorized by statute.

Comment 3: The problem with the court's approach here is that it buys into the notion implicit in the Restatement that once property owners commit themselves to a contractual scheme for common property, a subsequent court can view that agreement as an invitation to impose public policy considerations on this group as distinct from the community at large to achieve desirable public results. Particularly in the context of huge neighborhood covenant schemes, this is clearly an unwarranted interpretation of contract intent.

The common law notion of "changed circumstances" dealt primarily, if not exclusively, with reduction in the burdens imposed by a covenant. If in fact we start talking about increases in burdens based upon public policy, beyond those expressly agreed to by the bound parties, then essentially we're talking taxation without representation – government by court rule. Not a happy area for courts to enter, whatever their view about the ugly wrangling of selfish neighbors (abundantly decried here at the end of the opinion.) See the decision in *Evergreen Highlands Assoc. v. West,* 2003 WL 21373175 (6/16/03) (The DIRT DD for 6/19/03) (Association has power to add new provisions to declaration pursuant to a general power to amend, including provisions authorizing, for the first time, mandatory assessments.) But compare: *Armstrong v. The Ledges Homeowner's Assoc.*, 633 S.E. 2d 78 (N.Car. 2006) (The DIRT DD for 10/03/06) (Amendments of a declaration, even when the declaration expressly permits amendment, must be reasonable based upon circumstances surrounding original creation of the declaration and other factors. Court limits reach of expansion of association's assessment authority.)

ASSOCIATIONS; ASSESSMENTS; COLLECTION; LACHES: The failure to collect consistently set maintenance fees does not amount to an abandonment of a scheme where the association remains active and carries out some of its responsibilities and collects some of the assessments. Further, equitable doctrine of laches does not prevent a successor developer from attempting to collect maintenance fees that have long gone uncollected. ***Citizens Voices Association v. Collings Lakes Civic Association, 396 N.J. Super. 432, 934 A.2d 669 (App. Div. 2007)***, discussed under the heading: "Associations; Assessments; Collection."

The court held that for abandonment to occur, there must be a "clear indication of relinquishment," and "lackadaisical" enforcement or maintenance is not enough to constitute abandonment. The court further concluded that the equitable doctrine of laches did not prevent the successor developer from attempting to collect the maintenance fees from the encumbered property owners, even if its earlier developer had been lackadaisical in its collection efforts. It found no inexcusable delay.

ATTORNEY CLIENT; MALPRACTICE: Environmental malpractice case contains lessons for transactions lawyers. ***Barnett v. Schwartz, 2007 Westlaw 4328743, N.Y. Slip Op. 09712 (12/11/07).***

In 1992, Barnett and some business associates ("Barnetts") retained Schwartz to assist in leasing certain commercial property with an option to purchase. Barnetts intended to manufacture barbecue sauce on the property. The deal already had a lot of "legs" before Barnetts turned to Schwartz. He was retained in November and the lease was executed in December (the court does not give exact dates). In the course of discussions with the owners, Schwartz learned that a prior owner had been an industrial cleaner that had cleaned rags from the printing industry. Schwartz stated at trial, but Barnetts denied, that Schwartz had informed Barnetts of this fact.

Prior to the lease, on November 30, Schwartz sent letters of inquiry to the relevant county and federal environmental agencies inquiring whether they had any knowledge of environmental difficulties with the property, but never received any response. In fact, this letter stated that purchasers had been informed by the city environmental office that there might be a problem with a well on the premises. Barnetts expressly denied that they had ever been informed of these letters or their contents. Schwartz said that he had informed them. During the following December, on Schwartz's advice, and without any response to these letters Barnetts signed a lease with option to purchase that contained an "as is" clause.

Turns out that the *state* environmental agency, which Schwartz did not contact, had identified significant environmental problems due to the prior industrial cleaning activity and had put the property on a list of properties contaminated with "passive hazardous waste." Barnetts testified that they got some inkling of the problem for the first time through conversations with passers by two years after the lease had commenced.

Barnetts turned to Schwartz for advice, and they testified that Schwartz advised them that New York is a *caveat* *emptor* state and the landlords had not misrepresented anything about the property condition, and because in any event the lease contained an "as is" clause. In fact, Schwartz advised them, Barnetts testified, to go ahead and exercise the option because any clean up required would take no more than six months. [Where did Schwartz acquire that level of expertise, one asks (if indeed he said it)].

Apparently, Barnetts did not exercise their option, which then expired, but continued on the lease. Ultimately, pointing to the contamination, Barnetts stopped paying rent, complaining that even though the State was not demanding clean up, Barnetts were concerned about the health of their employees. Landlord then agreed to undertake a clean up and to extend the tenant's lease option at no rent until the clean up was complete. But the clean up took almost three years rather than six months, and the property finally was removed from the State list five years after Barnetts first suspended rent. All this time, apparently, Barnetts continued to occupy the property and ran their business without paying any rent.

After the clean up, the state environmental department indicated that it would be doing periodic testing of the air quality on the property, and this led Barnetts to conclude that the property never would be completely safe or free from "stigma." They again talked to Schwartz about suing the landlord, but he continued to advise him that they had no claim under New York law because of *caveat emptor* and because of the "as is" clause. Further, he told them that any cause of action was probably barred by the Statute of Limitations.

Barnetts ultimately acquired property elsewhere and moved their business. The landlord ultimately was able to resell the property for a price higher than the option price in the original lease/option.

Barnetts introduced evidence to the effect that if Schwartz had followed up on the inquiries begun by the two letters to environmental authorities, or if Schwartz had advised Barnetts to do an environmental assessment, the problems would have been identified and Barnetts would not have entered into the deal.

As you have figured out, Barnetts later sued Schwartz and his firm for malpractice. A jury found for plaintiffs and the judge denied a motion for judgment notwithstanding in favor of defendants on the grounds that the verdict was not supported by the evidence. The judge denied the motion and this appeal ensued.

Although the court is somewhat vague as to all the damages claims, some related to the payment of the rent for the two years preceding the discovery of the problem, and one assumes that there also were claimed damages related to the costs of relocating the barbecue sauce operation after eight years, since the Barnetts had been occupying the property rent free for the preceding five years. Schwartz argued on appeal that if Barnetts suffered damages, this resulted from their independent business decision to enter into the lease on an "as is" basis and to renegotiate the lease and remain on the property after they became aware of the environmental issue.

The court first turned to a technical issue of causation. It held that the trial court had been correct in instructing the jury that plaintiffs were only required to show that defendant's negligence was *a* proximate cause of their injuries, not that their injuries would not have occurred "but for" the negligence. Clearly, based upon precedent discussed by the court, there's an issue here, but, thank the lord and pass the barbecue sauce, it's not a real estate issue.

As to whether the conduct amounted to negligence, the court obviously was bound by the jury's determination in favor of plaintiffs, and thus could disregard defendant Schwartz's testimony that Barnetts knew of the problems from the start and made an independent decision to proceed. There was nothing in writing documenting that claim, and Barnetts denied it. So the question was whether Schwartz was negligent in not following up on evidence that he had obtained showing the possibility of some environmental problem with the well. The court held that this did amount to negligence. There was some testimony that had Schwartz diligently followed up his inquiry, he would have found out that the State environmental authorities had listed the property, and also some evidence that if Schwartz had disclosed this to Barnetts, they wouldn't have purchased.

Similarly, the court viewed as a jury issue Schwartz's argument that the Barnetts demonstrated that the environmental condition was of no concern to them when they extended the lease and option after learning of the condition.

A dissenter argued that the premises were not unsuitable for the use of the defendants at any time, as the facts arguably bear out, and that therefore Schwartz was not negligent in assisting and encouraging the tenants to enter into the lease option. In 1992, the dissent assumed there were no standards suggesting that tenants should do environmental studies prior to leasing, and no standards as to what such a study might entail.

Comment 1: Obviously this case is short on legal issue for real estate practitioners, but the editor ran the story nonetheless because it contains several clear malpractice traps that attorneys need to avoid. First, of course, one must be selective in picking clients. But not all lawyers have that luxury, so let's move on to more practical lessons.

Comment 2: The first important lesson is to read your client carefully to know how much care you must take in documenting information transfer to avoid malpractice claims.

It may be that, after some experience with a client, a lawyer may not be so particular about documentation. There is, of course, a desire to keep the client happy, to keep deals moving along with good pace, and to control the cost of the deal. Therefore, a lawyer might not document every conversation in order to insure that later there is a business record to support the lawyer's position as to who said what to whom. But at the beginning with a new client, and in significant deals in any context, lawyers must be aware that verbal warnings rarely will be provable in court. So any shortcuts in documenting conversations are potential malpractice traps.

The editor commenced work in a large firm in which every phone conversation got a memo to the file. Later, as a part time lawyer, he frequently worked without much secretarial help in informal settings, mostly for friends and acquaintances who had non standard deals. He remembers vividly a client coming to him desperate to close a squirrely lease option of client's property in a matter of days to stave off a bank's demands in another quarter. The deal involved an option on client's house that might be exercised three years later. At that time, the editor was dimly aware that if the client didn't live in the house prior to sale, the client lost some tax advantages. He told the client that the proposed deal raised tax complications that he didn't believe he had time to resolve in the framework for the close of the deal. The client said: "Don't worry, I've got my own tax advisers, taxes aren't your concern." But there was no tape running, and at the time these things were said, there was no file memo; indeed there was no file.

One all nighter later, there was a lease option agreement bound tight with anti-bankruptcy protections, security precautions, and other special features. The option was to be exercised within three years. But three years later, the optionee stalled for more time, got it, and eventually purchased. This took the deal beyond the owner's "safe harbor" for tax purposes. At tax time, editor got a visit from client's wife asking about the editor's malpractice coverage because their accountant had raised some tax issues. There was never a lawsuit, but there was gossip. [Yes, doctor, the editor still lives with the pain and relives the experiences twenty years later.]

Sometimes these problems are just part of life. As Tony Soprano's *consigliari,* the existentialist Sal, was wont to say: "What're you gonna do?"

But lawyers at all stages need to read situations and to know when one has a deal that demands documentation of all information transfers. Some firms now have a practice of purging email files periodically to protect their clients from litigation discovery claims. But does this expose the lawyers themselves when clients or others start pointing fingers at the lawyers?

Comment 3: A second lesson – never start what you don't finish. Even if the clients knew of the letters to the environmental agencies, how did the lawyer (without a lot of express warnings) let the deal close without following up? If the issue was important enough to ask, it was important enough to get an answer.

Comment 4: Lesson three: let the client own the deal. There is a little flavor in this case that the lawyer was holding himself out as a wily veteran full of practical wisdom that the clients ought to follow. The editor isn't sure this actually was true here, but he's seen it often enough. Good for the ego, bad for malpractice claims. The clients will still claim credit when things go well, but it is easier for them to hold the lawyer to blame when things hit the fan. This advice runs a little contrary to the above lessons, enjoining the lawyer not to get carried along by the tide. It is true that a lawyer must always give accurate and complete advice. And of course many clients rely heavily on lawyers to supply practical wisdom. But the most valuable advice the lawyer can give is: "It's your money and your life. You can listen to me for information, but make your own decision."

BROKERS; COMMISSIONS; VIOLATIONS OF LICENSEE REGULATIONS: A broker's violation of a statute or regulation that would authorize the Real Estate Commission to place the broker on probation, suspend or revoke license or to otherwise cause penalties, does not automatically deprive the broker of its commission, because it makes the commission agreement voidable, but not necessarily void. ***Exit A Plus Realty v. Zuniga, 395 N.J. Super. 655, 930 A.2d 491 (App. Div. 2007); September 5, 2007.***

A seller executed an exclusive listing agreement with a broker in connection with the marketing and sale of his house. During the exclusive listing period, the broker procured a buyer for the property, but the deal fell through. One day after the listing period expired, the seller and buyer revived the deal for a lower price and closed without paying the broker. The broker sued for its commission.

In its defense, the seller claimed that the broker violated a statute applicable to real estate brokers that requires brokers to provide sellers with a copy of the listing agreement on the date it was signed. It also prohibits a broker from allowing a seller to sign a listing agreement with a significant term missing. In this case, the seller claimed that the broker never gave him a signed copy of the listing agreement on the date it was signed. The seller also claimed that broker left blank a provision relating to the "extended protection" afforded to brokers if a buyer it has introduced to the seller buys the property within a certain period after the expiration of the listing agreement. The seller argued that due to its failure to comply with the statute, the broker should be barred from receiving a commission. The lower court agreed.

The lower court relied on the case of *Winding Brook Realty v. Platzer,* 166 N.J. Super. 575 (Law Div. 1979), a trial court decision that concluded that a broker who violates public policy as reflected in a statute is not permitted to enforce a commission agreement.

Notwithstanding the precedent, the Appellate Division reversed here, noting that the statute in question empowered the Real Estate Commission to regulate the conduct of brokers and to investigate their actions. The statute authorizes the Real Estate Commission to place brokers on probation, suspend or revoke licenses, and impose penalties on brokers that fail to comply with the statute.

The Court noted that the statute does not specify what remedy or discipline is to be taken against a broker that fails to comply with the statute, nor does it state that if the broker violates the statute, then the listing agreement is void. It found that a violation of the statute makes the listing agreement voidable, but not automatically void. The listing agreement could have been voided if the sellers suffered any prejudice by the broker's failure to leave a copy of the listing agreement, or by the insertion of the expiration date of the extended protection period at a later time. The Court found, however, that here, the seller had suffered no prejudice. The broker mailed a copy of the signed listing agreement to the seller the next day. The Court also noted that after the seller objected to the inserted date for the extended protection period, the seller proposed a shorter period and the broker agreed to the new date. Thus, since the broker substantially complied with the statute and the seller did not suffer any prejudice from the technical noncompliance, the agreement was enforceable.

The Court also noted that the seller, who received a benefit from the broker's efforts, also owed the broker a duty of good faith and fair dealing. Lastly, it questioned the seller's good faith in waiting until the listing agreement expired before agreeing to a price adjustment with a buyer introduced to him by the broker.

Comment 1: In *Huijers v. DeMarrais,* 14 Cal. Rptr. 2d 232 (Cal. App. 1992) a broker told some landowners that she had a party interested in purchasing their property. The client signed a listing agreement at a price of $325,000. The broker did not disclose at the time of listing that she already represented the buyer, and thus would be serving as a dual agent. Such disclosure was required by California law before execution of the listing.

Sellers later attempted to raise the listing price. Broker hesitated in agreeing to do so, and before this occurred there was a lengthy negotiation session attended by Sellers, Buyer and Broker. Buyer stated that it was California law that if Sellers refused to sell at the listing price (which Buyer was willing to pay) then Seller would owe the commission anyway. Just before Sellers signed, Broker delivered them a written dual agency representation. One of them commented that he might as well agree, since they were bound by the commission anyway.

A trial court found that the statement by the Buyer was correct and ordered specific performance and a commission. The appeals court reversed – first finding that the failure to reveal the dual agency until after the listing agreement was signed affected the seller's decision to list the property with this broker and that therefore the commission was forfeited, even though the buyer was willing to pay full listing price.

As to specific performance and damages to seller, the court remanded for greater analysis of the impact of the buyer's statement about sellers' obligation to pay the commission on the sellers' decision to sell. Was this a material misrepresentation by seller?

Comment 2: In this modern world of complex statutory disclosure requirements, the editor believes that the court has made the right choice in finding that not every breach of a detailed disclosure regimen is in fact a sufficient breach of fiduciary duty to warrant forfeiture of commission.

Of course, to conclude that a buyer must show injury before being able to refuse a commission may encourage brokers to flagrantly ignore their fiduciary responsibilities on the theory that they might get away with it if there turn out to be no real damages. This seems to be a bad approach as well, since we want brokers to take their responsibilities seriously.

Under the rule developed by the principle court here, the broker cannot be confident that any breach will lead to forfeiture of a commission, and therefore will still be under pressure to observe all the technical rules in the statute. Further, if the broker inadvertently fails to meet any technical requirement, the broker has an inducement to follow up and correct any incidental breach of statutory duty as soon as possible to minimize the likelihood that the commission will be lost. This is a nice compromise. The many statutory disclosure rules indeed do deal with an articulation of fiduciary responsibilities. But they are so complex that there will be many minor violations not representing any attempt at fraud or chicanery and leading to no real injury. To impose the commission forfeiture requirement in every case injects an inappropriate penalty feature that is not set forth in the statute and may lead to pressure on the legislature to soften the rules themselves or to brokers to take pains to disguise violations.

CLOSINGS; DUTIES OF CLOSING AGENT; DISCLOSURE: A lawyer closing a purchase and loan transaction has no duty to buyer to disclose information known to lawyer concerning defects in title unless buyer has retained lawyer as a title insurer or agent or court concludes that purchaser, in addition to lender, can be regarded as a client of lawyer. ***Davis v. Montenery, 2007-Ohio-6221, 2007 Westlaw 4145989 (11/15/07)***.

Davis contracted to buy agricultural land that had a barn. There was an issue about access across a neighbor's land to provide convenient access to the barn and 21 acres around it, which otherwise were separate from the main parcel that Davis was buying. Sellers, many years before, had transferred the neighboring property and reserved a recorded easement to get to the barn. But soon after reserving this easement, sellers had agreed by separate instrument to relinquish their easement and replace it with a personal license terminating on sellers' deaths.

Davis asked whether the existing road to the barn, across the neighboring property, would be available to him. The real estate agent inquired of the surviving seller, who told him of the easement deed, and the agent actually went to the land records office and got a copy of the deed and presented it to buyer.

Subsequently, Davis agreed to buy the property and sought a mortgage loan from Bank, which retained lawyer Thomas to "do the title work." Thomas found both deeds and apparently so informed Bank. Thomas later testified on deposition that his job was to be sure "the title was clear." Thomas didn't inform Davis of the easement problem.

At deposition, Davis indicated that Thomas had represented or worked with Davis on a number of prior real estate deals and that he asked the bank to retain Davis to do the title work on this deal. Clearly there were meetings prior to closing between Thomas and Davis, and Davis even claimed that at closing, Thomas had informed him that the easement was good, even though in fact it expired upon transfer to Thomas. In addition, Thomas' title notes identified Davis as the client, although Thomas stressed that this meant the bank's client, not Thomas'.

The trial court found that Thomas did not represent Davis, was paid by the bank to do the bank's title work, and granted summary judgment to Thomas.

On appeal, the Ohio Court of Appeals reversed, finding sufficient evidence to overcome summary judgment that Thomas in fact represented both Davis and the Bank in this transaction. ["Never a good idea," grumps the editor.]

But Davis also argued that Thomas had a duty of care to disclose accurate information to parties relying upon Thomas' work in the context of a business transaction even if such parties were not Davis' legal clients.

The court noted that established (1910) Ohio precedent stood for the notion that a title abstractor's duty is only to the person that employed him. It admitted that at least one prior appellate panel had questioned the appropriateness of this rule in the modern context. It noted that the Ohio Supreme Court had thrown out the "privity" rule in connection with claims against an accountant for professional malpractice where a plaintiff's reliance on the professional performance is foreseeable. The court here acknowledged that Davis' reliance on Thomas' work in this case "may have been both foreseeable and reasonable," but that the Ohio Supreme Court had not overruled its abstractor liability requirement for privity, and the fact that it had done so in the context of an accountancy case was no basis to ignore established precedent here.

Ironically, Davis' claim against both the seller and the real estate agent were dismissed because Davis stated categorically that he did not rely on their statements that there was an easement but instead said, "I sent to Mark Thomas on that." Turns out to have been the wrong place to go, at least unless and until the Ohio Supreme Court takes another look at this issue.

Comment 1: It appears that the court is only willing to entertain plaintiff Davis' claim if he can show that Thomas functioned as his lawyer. It seems to the editor that the existing record suggests other basis for liability here. Davis claimed that he went to Thomas specifically to find out about the easement and that at closing, after Thomas had identified the easement release document, rendering the first easement document void, Thomas still told Davis that the easement was good.

How can it be that a practicing lawyer has no duty to disclose honestly and fully information asked him by any party involved in a transaction of which the lawyer is a part? Certainly absence of privity is no defense against outright fraud.

Comment 2: Beyond the question of fraud, the editor also is inclined to the view that where a professional utters an opinion in the context of a business transaction with full knowledge that others in the transaction are relying upon that opinion, the professional ought to be liable if the opinion is negligently prepared or rendered. Particularly in modern real estate transactions, many professionals are called upon to provide critical information with full knowledge that they are the only source of this information. The transaction wouldn't go ahead without their information, and the party retaining them clearly expects that others in the transaction will rely upon this lawyer's work. The editor's view, obviously, extends beyond abstractors.

The editor understands the Pandora's Box argument here. Clearly there must be some rational control on who can rely upon what a professional does. Third parties unrelated to the transaction perhaps ought to be excluded, as should parties who in fact are not relying on the professional's work in connection with their decisions related to the transaction. But there has to be an area of responsibility within the transaction that goes beyond issues of privity.

CONSTITUTIONAL LAW; DUE PROCESS; TAKINGS: Ordinance prohibiting property owners from owning farm animals does not constitute a taking. ***Litva v. Village of Richmond, 172 Ohio App. 3d, 349 (2007).***

Plaintiffs owned property in Richmond, Ohio and kept farm animals on their property. When Plaintiffs purchased the land, there were no ordinances or restrictions prohibiting the housing of farm animals on their property. Subsequently, the village passed an ordinance that prohibited the "keeping, harboring, fencing, penning, pasturing, or stabling of . . . fowl and farm animals." The village passed another ordinance permitting those who already owned farm animals to keep their animals as long as they registered them with the village.

Plaintiffs argued to the trial court that the legislation hindered their farm animal businesses. The court held in favor of City on summary judgment, determining that the ordinances were enforceable, although Plaintiffs may maintain the *same number* of farm animals they possessed on the effective date of the ordinances.

Plaintiffs appealed, arguing that the ordinance constitutes a taking under the Fifth Amendment. The appeals court noted that because Plaintiffs failed to raise this argument during summary judgment, they are precluded from bringing it now. The court continued, however, to discuss in *dicta* whether the ordinance constituted a taking and determined that it did not.

The court affirmed the trial court's decision but modified the portion of the decision that held Plaintiffs could only own as many farm animals they possessed at the effective date of the ordinance. The court stated that the ordinance's only restriction on the owners was to register their animals, and consequently, there should be no such restriction on how many animals they may possess.

CONSTITUTIONAL LAW; DUE PROCESS; TAKINGS; MINING RIGHTS: Denial of mining permit does not constitute regulatory taking, though mineral estate may be relevant parcel for compensable regulatory taking if purchased separately from other interests. ***Shelly Materials, Inc. v. Clark County Board of Commissioners, 875 N.E.2d 59 (Ohio 2007).***

In 1998, Shelly, in the business of sand and gravel extraction, purchased a 306.057 acre tract of land in Moorefield Township, Ohio, to mine subsurface sand and gravel deposits. The property was zoned A-1, which allows for resource and mineral extraction as a conditional use. Eight subdivisions with more than two-hundred residential lots surrounded the property. A year after purchasing the property, Shelly applied for the conditional-use permit to mine sand and gravel for twenty years. The Clark County Board of Zoning Appeals (BZA) denied Shelly's application because Shelly had not complied with certain zoning regulations.

The Court of Common Pleas affirmed the denial of the permit. The Second District Court of Appeals determined that some of the BZA's findings were not supported by credible evidence, but upheld its determination that Shelly had not demonstrated that its operations would not be detrimental to the vicinity or surrounding properties.

Shelly then filed a complaint with the court of appeals for a writ of mandamus to compel the commissioners to begin appropriation proceedings, alleging the merit denial amounted to an involuntary regulatory taking. The court denied Shelly's motion and denied the writ. The final clause of the fifth amendment to the United States Constitution provides that private property shall not be taken for common use without just compensation. U.S. Const. amend. V. The denial of a permit allowing a certain use of the property could constitute a taking if the effect of the denial is to prevent *all* economically viable use of the property.

Shelly purchased the property with knowledge that a conditional-use permit was required to mine for sand and gravel on the property. The existence of the permit implied that permission for mining may be granted, or denied. When the permit application was denied, the property did not lose *all* economic value, so a taking did not occur. In comparing the current case with *State ex rel. R.T.G., Inc. v. State*, 98 Ohio St. 3d (Ohio 2002), the court noted that Shelly purchased the land in its entirety and the deed granted fee simple title. Because Shelly did not purchase a mineral estate separately from the relevant parcel, for evaluating a regulatory takings claim, the property should be considered as a whole. Shelly purchased fee simple title, and there are other potential economically viable uses for the land.

Comment: Of course, the fact that the parcel overall retained substantial value killed the takings claim in the absence of substantial investment in the parcel in the belief that mining was permitted.

But the editor is not certain of the other grounds for denial – the fact that plaintiff was aware that a conditional use permit was required. Typically, a conditional use permit is available as a matter of right if certain discrete and clearly stated requirements are met. Unlike a zone change, such a permit is not a complete exercise of overall land use policy discretion. If the denial of the permit had resulted in plaintiffs suffering a complete loss in value in the property, the editor believes that a taking would have occurred.

CONDOMINIUMS; ASSOCIATIONS; CONSUMER FRAUD ACT: Even though a condominium association may not have been formed at the time the project's builders or suppliers acted in a way so as to violate the state Consumer Fraud Act, the association will still have standing to bring an action against the builder or supplier because those parties were clearly on notice that the association would be the end-user and was the intended beneficiary for work to be performed. ***Port Liberte Homeowners Association, Inc. v. Sordoni Construction Company, 393 N.J. Super. 492, 924 A.2d 592 (App. Div. 2007).***

EASEMENTS; CREATION; PRESCRIPTION: While a road once designated as a "public road" can be abandoned as such, a prescriptive easement may survive that abandonment with respect to private parties who use the road to access adjacent properties, preventing the "owner" of the road from erecting barriers which wrongfully prevent those private parties from accessing their properties. ***Jameison v. Eagle Rod & Gun Club, Inc., ___ S.W.3d ___ (Ky. Ct. App. 2007)***, discussed under the heading: "Easements; Termination; Abandonment; Prescription."

EASEMENTS; CREATION; PRESCRIPTION; HOSTILITY: Arkansas case holds that extended use of road without permission is not presumptively adverse. It is up to prescriptive to provide additional evidence of hostility. ***Baysinger v. Biggers, 200 Ark. App. 109, 2007 WestLaw 2964361 (Ark. App. 2007).***

This very brief opinion pretty much only says what's in the caption, with very little analysis. But it is significant that the court reversed the finding of the trial court that an easement by prescription had been established.

Claimant used the road without permission for the prescriptive period. Then the alleged servient owner put in a gate, which restricted the claimant's use of wide bed pickup trucks, such as it had been using. Here was the court's analysis of the hostility issue:

"[A]ppelle had continuously used the roadway for a period in excess of seven years. However, there was no evidence, other than the length of use, to establish that appellant knew or should have known that the use was hostile. The only evidence at trial was that appellee began using the road to access his property in 1961 and that there had been no objection.. . . testimony at the hearing was exclusively directed to the extent of the use rather than the nature of it."

The court stated (correctly) that time alone will not suffice to transform permissive use into legal title. It noted that this road was over forested lands and "was described as an old timber road." The court distinguished cases that involved evidence of the general public using the road, apparently viewing these cases as involving a higher likelihood that such use would be deemed adverse to true owners interest.

Comment 1: This simple little case perhaps illustrates a growing tendency nationwide to be more conservative about recognition of adverse possession claims. In fact, the court refers to adverse possession case law and analysis, even though it's working only with a claimed prescriptive use right.

In both cases, though, modern theorists seem to be more offended than those of prior years with the notion that a landowner might be saddled with a permanent imposition on his rights for what the landowner was as nothing more than a "neighborly accommodation."

At one time, the existence of a prescriptive farm road across someone else's acreage did not represent much of an inconvenience. Now, however, courts and theorists are well aware how quickly development can descend upon a neighborhood. What was once a hardly noticed back road can suddenly become a major impediment to development of the owner's tract.

Comment 2: For a case where an arguably neighborly accommodation (permitting a mailbox to exist for fifty years) ripened into a prescriptive right, see *Gajewski v. Taylor*, 536 N.W.2d 360 (N.D. 1995) (The DIRT DD for 1/11/96). Some jurisdictions, such as New Mexico, assume that roads across unfenced property are permissive, but this is not universally true: See *Wilson v. McElyea*, 815 So. 2d 462 (Miss. App. 2002) (The DIRT DD for 10/1/02) (Where there is no evidence as to whether a long continued use originated with permission or not, the court will assume that the use was adverse.); *Harambasic v. Owens*, 920 P.2d 39 (Ariz. Ct. App. 1996) (The DIRT DD for 1/30/97) (Even in open country, adverse claimant's use of an easement over land of another in open, visible, continuous and unmolested manner establishes presumption that claimant's use is hostile and notorious, as opposed to being permissive, and landowner's failure to rebut presumption allows court to find existence of easement by prescription.)

Of course, actual permission can prevent a presumption of hostility, even if permission had been granted by a prior owner: *Rettig v. Kallevig*, 936 P.2d 807 (Mont. 1997) (The DIRT DD for 9/30/97); also see *Wilson v. McElyea,* 815 So. 2d 462 (Miss. App. 2002) (*supra*).

Comment 3: Of course, there are other cases that reflect views more akin to those of the Arkansas court here. *See, e.g.: Collins Trust v. Allamakee County Bd. of Supervisors,* 599 N.W. 2d 461 (Iowa 1999). In Iowa, the simple existence of continuous unpermitted use does not give rise to a presumption of hostility; a prescriptive claimant must demonstrate further some evidence of claim of right, and such requirement can be supplied by acts of maintaining and improving a claimed prescriptive right of way. (The DIRT DD for 4/12/00)

EASEMENTS; TERMINATION; ABANDONMENT; PRESCRIPTION: While a road once designated as a "public road" can be abandoned as such, a prescriptive easement may survive that abandonment with respect to private parties who use the road to access adjacent properties, preventing the "owner" of the road from erecting barriers which wrongfully prevent those private parties from accessing their properties. ***Jameison v. Eagle Rod & Gun Club, Inc., ___ S.W.3d ___ (Ky. Ct. App. 2007).***

The Eagle Rod & Gun Club (the Club) purchased a 100-acre farm adjoining the Jameison property. The Club's property was essentially landlocked, but when Club members viewed the property in anticipation of purchase, they gained access to it by traversing the Jameison property over an unpaved route approximately one mile long. After the Club purchased the farm, the Jameison's erected a locked gate on their property and placed other barriers on the road to restrict Club members' access.

The Club filed suit, claiming that the road was a public road which the Jameison's were prohibited from blocking. The circuit court judge found that the road was "a remnant of an old public road," that it had not been abandoned as such, and that by blocking the road, the Jameison's were in violation of the applicable statute. Therefore, the judge entered a permanent injunction which ordered the Jameison's to remove the obstructions and to refrain from erecting obstructions in the future. On appeal, the general issues addressed by the court were (1) whether the road in question constituted a "public road"; (2) the circumstances under which a public road can be abandoned by the general public as such; and (3) if so abandoned, whether the abandonment applies as against private parties who use the road.

With respect to the first issue, the court began by noting the long-standing principle that "a public road can . . . be established by general and long continued use of a passway by the public[.]" After reviewing the evidence in the record and applying a "clearly erroneous" standard, the court refused to set aside the judgment of the circuit court on this issue, concluding that the road was once a public road.

Next, the court addressed the Jameison's argument that the road was abandoned by the general public as a public road. Once the public acquires the free use of a roadway, "it may abandon that right by a long period of nonuse[.]" Citing *Sarver v. Allen County*, the court noted that the public must abandon the use of a public road for 15 years in order for the road to lose its status as a public road. The evidence in this case showed that since 1945, the road was used only by the owners of the surrounding properties, and therefore it had been abandoned as a public road.

However, the court also noted that if a subject road was once a public road, it follows that the road "came to that status through 'public use [that] ripen[ed] into a prescriptive easement'." In other words, "[t]he prescriptive easement for *public* use necessarily subsumed the *private* prescriptive use of the same road by the owners of the properties adjoining it." Therefore, while a road may be abandoned as a public road, a prescriptive easement may survive as to private parties who own land adjacent to the road, as well as their invitees. In the present case, the evidence showed regular use by the owners of those adjoining properties, and therefore the prescriptive easement survived in this case, despite the fact that the road ceased to be a "public road" years ago. Based on the foregoing analysis, the court affirmed the permanent injunction against the Jameisons.

EASEMENTS; TERMINATION; PRESCRIPTIVE BLOCKAGE: Planting of trees in easement is sufficient adverse use to terminate that portion of servient area, and special six year statute on "injury to incorporeal hereditaments" sets the appropriate measuring period, rather than longer adverse possession statute. ***Link v. Pottle, 654 S.E. 2d 64 (N.Car. App. 2007)***.

In an island community, a number of subdivided lots benefitted from a thirty foot easement over two lots that lay between the benefitted lots and the public road. Within the preceding eleven years, owners of the two servient properties had planted trees and landscaping within the thirty foot right of way. All of this, the inland owners alleged, interfered with access for large trucks, moving vans, and the like, providing services to their properties, and they sought injunctive relief clearing the easement.

The servient properties responded that they had maintained the obstructions for over six years and that therefore they were entitled to a finding of prescriptive blockage, permitting them to maintain permanently the obstructions of the easement. Section 1-50(3), North Carolina general statutes, requires that an action for injury to any incorporeal hereditament be brought within six years. The dominant owners argued that the twenty-year North Carolina statute of limitations on adverse possession ought to control.

Of course, the literal language of the statute applied to blockages of "incorporeal hereditaments," which, according to common usage and dictionary definitions, includes easements. But plaintiffs argued that it is one thing to claim a prescriptive right to block an easement and quite another to assert a permanent right – virtually ownership. It cited to two cases in which landowners had built permanent structures across property lines and argued that the three-year statute on trespass applied to bar further claims. The court rejected this argument and held that a claim of the right to maintain a permanent structure was a claim of ownership, and that the twenty-year North Carolina adverse possession statute would apply. Similarly, plaintiffs argued, the permanent right of blockage alleged here effectively returned ownership of the blocked area back to them.

Presumably, the plaintiffs argued to the appeals court that the statute aimed to apply the shorter statute of limitations to continuous activities and uses that do not amount to the establishment of permanent physical rights. Of course, many incorporeal hereditaments are use covenants and similar restrictions, and certainly the typical "injury" such restrictions is not a permanent improvement.

Nice as this distinction might be, it failed to convince the court, which held that the statute's literal reach applied to the defendant's activity here. Six years is all that is required. As the trees had been planted earlier than six years before suit, they stayed.

Comment 1: Most jurisdictions, the editor believes, do apply the same statute of limitations to the establishment of prescriptive easements and to blockage of easements and covenants as they do to adverse possession generally. In Missouri, for instance, it's all ten years. Some statutes that have different statutes for prescriptive easements than for adverse possession, and presumably the same statute would apply to prescriptive blockage. In some of these the adverse possession requirement is longer, but in some it is shorter. *See, e.g.: Randolph Town Center, L.P. v. County of Morris,* 864 A. 2d 1191 (N.J. Super. 2005) (The DIRT DD for 3/29/05) (New Jersey court holds that statute of limitations for prescriptive easement may be as long as sixty years, and never less than thirty years, although adverse possession period is twenty years.)

The North Carolina legislature chose to subject its citizens to this rather short prescriptive blockage statute, likely because of some sad story involving some sad legislator a number of years before. Whatever the reason, it's the policy of the state, and the editor believes the court was correct in divining and applying the probable intent of the statute. But what a terrible result.

Another analysis the court might have used, however, would be to conclude that the trees didn't begin to establish prescriptive blockage until they in fact interfered with the needs of the neighbors. In other words, if, prior to the dispute arising, the neighbors had had no need to protest the encroachment, and that consequently no hostile claim had arisen, as the servient tenant had the right to use the servient property for landscaping, including trees, until such time as there was interference with the needs of the dominant owners. For an interesting application of this theory, see *Sabino Town & Country Estates Association v. Carr,* 920 P.2d 26 (Ariz. Ct. App. 1996). (The DIRt DD for 2/3/97) (Even fencing off of motor vehicle access across easement by servient owner does not extinguish recorded easement for motor vehicle access when servient owner continues to allow pedestrian and equestrian access. Dominant owner is later able to get fence removed to accommodate new need for vehicular access.)

Comment 2: Compare: Silacci v. Abramson, 53 Cal. Rptr. 2d 37 (Cal. App. 1996) (the DIRT DD for 9/25/96) where a landowner attempted to establish an "exclusive prescriptive easement right" in order to take advantage of the prescription statute in California, which permitted prescriptive easements to be established in five years without evidence of payment of taxes. Although California's adverse possession period is equally short – five years – the claimant must show payment of taxes. The court rejected the claim, holding that where a permanent exclusive right is sought, we have an adverse possession claim. The reasoning is similar to the argument made by the plaintiff in the instant case, but the problem is that the defendants in the instant case were *already* the owners of the servient land, and were merely attempting to establish a right to block, not a new permanent right of ownership.

Comment 3: Here are some puzzlers:

(1) What if the trees blow down or otherwise disappear? Is the prescriptive easement to maintain *these* trees, or any trees within the area occupied by the original obstructing trees? The editor presumes that a court would permit replacement.

(2) Can the trees grow further into the easement area? Note that traditionally the scope of a prescriptive easement is limited to the original area occupied by the prescriptive use. *Compare: Koresko v. Farley*, 2003 WL 23318662 (Pa.Cmwlth.) (The DIRT DD for 5/6/04) (In a case of first impression, the Commonwealth Court of Pennsylvania decides that a prescriptive easement did not arise from encroaching tree roots and overhanging branches.)

(3) For that matter, what is the width of the prescriptive blockage? The maximum spread of the branches over the ten years of prescriptive activity, or the minimum spread within the most recent six years, or some other measure. Could make a big difference to those moving trucks taking away the belongings of the neighboring owners whose properties have suddenly lost significant value through their neighbor's land grab.

EMINENT DOMAIN; DAMAGES; ABANDONED PROCEEDING: Recoverable costs in an abandoned condemnation action can only be for costs incurred as a result of being named in the condemnation action by the condemning authority and the costs incurred in participating in earlier activities, such as attending municipal board sessions are not recoverable following abandonment of the action by the condemning authority. ***Township of West Orange v. 769 Associates, LLC, 397 N.J. Super. 244, 936 A.2d 1023 (App. Div. 2007).***

EMINENT DOMAIN; DAMAGES; CONSEQUENTIAL DAMAGES: As a matter of first impression in the District of Columbia, the D.C. Court of Appeals finds that the owner of a gasoline service franchise business, leasing land taken by the District by eminent domain, is not entitled to compensation for business losses, goodwill, and other consequential damages under the Fifth Amendment. ***Mamo v. District of Columbia, 934 A.2d 376 (D.C. 2007).***

Plaintiff occupied a BP service station under a BP franchise. When the District resolved to obtain plaintiff's property by eminent domain, the District's Project Director assigned to carry out this project wrote a letter to Plaintiff's attorney stating that "your client will be properly compensated for his leasehold interest, his business, and his goodwill."

In fact, under the terms of the BP lease, BP could terminate the lease in the event of condemnation, which it promptly did (in advance of the actual condemnation.) Thus, as of the time of condemnation, Plaintiff had no interest in the property taken and the District negotiated a condemnation award to BP and paid BP, giving Plaintiff nothing.

Plaintiff brought a lawsuit alleging: (1) Plaintiff is entitled to damages for loss of a valuable business and goodwill under cases interpreting the Fifth Amendment of the U.S. Constitution; (2) Plaintiff is entitled to a split of the damages under the terms of the Federal Petroleum Marketing Practices Act (15 U.S.C. sec. 2802(d)(1)). (3) In any event, Plaintiff is entitled to compensation for his "leasehold interest, business and goodwill," due to estoppel based upon the letter promising such compensation described above.

The appeals court affirmed the lower court's denial of relief to Plaintiff.

The court found that the U.S. Supreme Court decisions interpreting the Fifth Amendment make quite clear that "the sovereign must pay only for what it takes, not for opportunities which the owner may lose." Things like loss of good well or other consequential losses that would ensure from the sale of the property to someone other than the sovereign might be taken into account in figuring the price for such a sale, but need not be taken into account in eminent domain.

Plaintiff cited a case involving a temporary taking in which the landowner was given compensation for business interference. The court noted, however, that special considerations apply in the case of a temporary taking, as the condemnee is left with few options to open the business at another location.

As to the Petroleum Marketing Act, the Act does provide that in the case of a termination or nonrenewal based upon condemnation (among other things) the "franchisor shall fairly apportion between the franchisor and franchisee compensation, if any, received by the franchisor based upon any loss of business opportunity or good will." But the predicate of this statutory provision is that the franchisor in fact receive compensation for loss of business opportunity or good will. Although the court didn't have before it the exact record of the award to BP here, the court concluded that there was no evidence of any award for good will. But more to the point, the court indicated that at the time of such award, the franchisor had already terminated the lease pursuant to a lease provision permitting it to do so in the event of a taking. The court commented that in such cases the lessee has already "bargained away" any right to share in the compensation award, and is outside the protection of the Petroleum Marketing Act.

The estoppel argument did require serious thought, of course, as the letter from the Project Director categorically promised compensation for loss of the lease and good will. But the court concluded that the Project Director was not able to bind the District. [Why not?] Moreover, the court concluded that the Plaintiff had shown no reliance upon such representations.

Comment 1: The holding on the meaning of "just compensation" under the Fifth Amendment, is, so far as the editor knows, accurate and reasonably well established, despite the few cases cited by Plaintiff to bulk up a hopeless position. Of course, some states and some statutory condemnation provisions may alter the general rule.

Comment 2: The reading of the Petroleum Marketing Act strikes the editor as a bit severe. As the editor understands, the purpose of the Act is to protect franchisees from overreaching by franchisors in connection with least terminations that leave franchisors overcommitted to the franchise and suffering significant lost investment. The Act certainly could be read to override a lease provision termination the lease in the event of condemnation, and the editor wonders whether this hasn't occurred elsewhere, or whether it might so occur in the future. But in any event it is unlikely that BP in fact got any good will compensation, so the point is moot here.

Comment 3: Plaintiff had the burden to show how he had relied on the letter by the Project Director. The court cites no evidence of such reliance. Obviously this was a significant failure by Plaintiff. But what could Plaintiff have shown? Likely the letter was written to pacify potential political opposition to the proposed eminent domain taking, even though it was already well down the road by the time the letter appeared. Citizens who feel that their land is being taken unfairly often will throw themselves in front of trains to prevent the eminent domain project from proceeding. Likely they'll not stop the project, but they'll often delay it, and embarrass the involved political interests.

But is failure to undertake political opposition to a proposed public project the kind of "reliance" that supports an estoppel? Probably not. Better if the Plaintiff, anticipating an award of some kind, committed itself economically to a relocation plan that required the money that such an award might provide. If that had happened here, it is likely the court would have known about it.

EMINENT DOMAIN; DAMAGES; ESTOPPEL: Statement by public agency project director that lessee on land scheduled for condemnation will receive compensation for loss of lease and goodwill does not bind the agency in the absence of delegated authority of the director to make such statement and in the absence of demonstrated reliance upon such statements by lessee. ***Mamo v. District of Columbia, 934 A.2d 376 (D.C. 2007)***, discussed under the heading: "Eminent Domain; Damages; Consequential Damages."

EMINENT DOMAIN; POWER TO CONDEMN; DUTY TO NEGOTIATE: City failed to make good faith effort to agree on just compensation with landowner before exercising its rights under Eminent Domain Act. ***City of Chicago v. Zappani, 877 N.E.2d 17 (Ill. App. Ct. 2007).***

In April 1995, the City of Chicago approved amendment number 10 to the development plan for the Central West Redevelopment Area, authorizing the city to acquire 167 properties, including three parcels owned by Zappani. Eight years later, the City mailed a certified form letter to Zappani informing him the City Council had authorized acquisition of one of the parcels, offering $110,000. The letter stated that the City's offer would remain open for ten days from the date of the letter, after which the City would assume Zappani was not interested in voluntary sale, and would commence legal proceedings under the Illinois Eminent Domain Act (EDA).

The certified return receipt signed by Zappani was dated May 23, 2003, a month after the letter was sent. Similar certified form letters were mailed to Zappani regarding the two other parcels he owned: one dated June 18, 2003, and signed for June 20, 2003 offering $140,000; and, another dated February 11, 2004, and signed for February 23, 2003 offering $68,000. All three letters stated that, "[t]he amount of the offer is the amount believed by the City of Chicago to be just compensation for the subject property and is not less than its approved market price…," but included no supporting information or report.

Zappani did not respond to any of the letters, and the City commenced three separate condemnation actions. On December 20, 2005, Zappani filed a traverse and motion to dismiss directed at all three cases on the grounds that the city had failed to make a good-faith offer of settlement to purchase, as required under the EDA, before filing for condemnation. The trial court rejected Zappani's traverse and motion to dismiss, ruling against Zappani's claim that the City had failed to negotiate in good faith.

At a May 23, 2006 case management conference, the City updated its offers to Zappani to reflect secondary appraisals completed around the dates that the condemnations were filed. The offered price for each property increased dramatically: for one property, from $110,000 up to $180,000; for the second, from $68,000 up to $135,000; and, for the third, from $140,000 up to $290,000.

The trial court concluded there were no factual issues for trial, and set the orders for condemnation at $180,000, $140,000, and $305,439 respectively, allowing input from Zappani's own appraisal. Zappani appealed, claiming the City failed to negotiate in good faith.

Held: *Reversed*. Condemnation could not proceed (apparently).

The EDA requires potential condemnors to engage in good-faith negotiations with the landowner before filing a condemnation action. *Dept. of Trans. Ex rel. People v. 151 Interstate Road Corp.*, 810 N.E.2d 1 (Ill. 2004). The finding of good-faith action is a question of fact, and the trial court's decision may only be reversed if it is against the manifest weight of the evidence. The appeals court ruled that the trial court's ruling was against the manifest weight of the evidence for three reasons. First, the City's first mailed offer prices were low, substantially below their subsequent appraised and offered prices. The court noted particularly that the City, in fact, agreed by subsequent appraisal that the value at time of filing the complaint, which was only a few months after the letters were sent, was significantly higher than the value set forth in the letters, placing the accuracy of the value in the letters in great doubt. Thus, the court concluded that the City first offered Zappani significantly below fair market value, which does not constitute good-faith negotiation. *See City of Naperville v. Old Second Nat'l Bank of Aurora*, 763 N.E.2d (Ill. App. Ct. 2002).

Second, the ten-day window that Zappani had to contact the City was inadequate, particularly given that Zappani did not even receive two of the letters until after this time period expired. The City knew this.

Finally, while there is no specific requirement that the City attach appraisal reports to the offer letters, Zappani had no information regarding how the City determined its price. Attaching the appraisal reports would have been reasonable and a showing of good faith.

Comment 1: Note that the court did not in fact require any specific practice going forward, but the three flaws it found here, one supposes, will be remedied in the future. They seem pretty obvious if the city really is negotiating in good faith.

Comment 2: What exactly is the remedy? Requirement for a new lawsuit? The court doesn't really discuss whether valuation must be at time of filing of a complaint or at time of taking. The trial court rejiggered the appraisal values in approving the condemnation, but refused to permit the defendant time to submit updated appraisals as of the time of taking. We really don't get an answer as to what time is appropriate. It would seem that, since the City must negotiate in good faith *before* initiating a condemnation suit, that the currently filed suit must be dismissed, and in any event new negotiations must begin with updated values. Zappani's attorneys earned their fees here.

Comment 3: Zappani also argued that the condemnation was inappropriate because the finding of blight that supported this condemnation had occurred twenty years earlier, and there had been significant development in the area since that time. It's too bad the court didn't reach that issue.

Of course, the City must have some time to get its "ducks in a row" to negotiate redevelopment of an area declared blighted, and must be able to rely upon its earlier blight findings to do that. But should this "window of opportunity" last forever? Or is there some point at which we must conclude that a new justification for the taking must occur? This court won't tell us.

ENVIRONMENTAL LAW; REMEDIATION: There is no New Jersey constitutional bar that applies to the Department of Environmental Protection's removing a property owner as the party who would perform environmental remediation of contaminated property and substituting itself instead, but, because of the potential significant financial consequences for the owner that is removed, the Department does not have the unlimited ability to do so. ***NL Industries, Inc. v. New Jersey Department of Environmental Protection, 397 N.J. Super. 127, 936 A.2d 469 (App. Div. 2007)***.

ESCROWS; UNJUST ENRICHMENT: Where escrow agent distributes sale proceeds to borrower instead of using them to clear mortgage lien from property, and later reimburses title insurer that insured over the problem, escrow agent may recover from original seller of property who received the proceeds on a theory of unjust enrichment unless escrow agent was unreasonable in concluding that it had a reimbursement obligation to title insurer. ***Hill v. Cross Country Settlements, Inc., 2007 Westlaw 4225135 (12/3/07)***.

Sasso had transferred her home to Hill, her daughter, but reserved a life estate with power to encumber. Sasso entered into a home equity mortgage loan with Provident in 1999, and in 2002 she refinanced that loan, also with Provident. At that time, Provident recorded a new deed of trust for the refinancing loan and issued a certificate of satisfaction. (The record is unclear whether the certificate was recorded or whether it should have been).

A year later, Sasso died. Hill made the payments on the Provident loan for a year, and then sold the property. Cross Country provided escrow services in connection with the sale.

Noting the presence of a recorded deed of trust, Cross Country contacted Provident, but apparently ran into some difficulty communicating with Provident (possibly a subprime servicer involved?) Cross Country asked Hill for information about the loan. Hill (apparently through good faith mistake) gave Cross Country the number from the original 1999 loan. When Cross Country contacted Provident about that loan, it got back a letter stating that the loan had been satisfied on October 30 of 2002 and a certificate of satisfaction sent to borrower in January of 2003. Cross Country wasn't sure about this answer, because it was looking at a deed of trust recorded October 25 of 2002. Thus the loan would have been satisfied only five days after it had been made. So it asked Provident again, and got back the same letter with essentially the comment: "asked and answered."

Cross Country did not seek a formal confirmatory release or certificate of satisfaction.

People don't seem to agree about what happened at closing. Cross Country's affidavit claimed that it asked Hill about the Provident Loan and she then stated that she must have given them a number for a credit card account. Cross Country claimed that Hill affirmed that the payoff letter was accurate (Hill may have disagreed with this statement). In any event, Hill then signed an owner's affidavit stating that there was nothing adversely affecting the title to the premises except as set forth in the affidavit. Of course, Hill did not list the current Provident mortgage on that affidavit. The trial court stated in one of its rulings that there was no indication that Hill had in fact misrepresented anything deliberately. The high court, in a footnote, comments dryly that its not sure what the trial court made of the fact that Hill certainly knew that the Provident loan hadn't been paid in 2003 and still existed since she'd been making payments on it for the preceding year.

Cross Country then closed the deal and, as agent for Stewart Title, insured Buyer's title free of the Provident deed of trust. It disbursed all the sale proceeds to Hill and, of course, paid nothing to Provident. Two months later – surprise!!! Here comes the Provident request for payoff in the amount of $70,000. Cross Country demanded that

Hill supply the payoff money. When she didn't respond, Provident threatened foreclosure. Buyer turned to the title insurer, which paid Provident "without apparent protest or mounting a defense to the foreclosure on behalf of . . . its insured." The high court commented that the Stewart policy was not in the record, so it couldn't evaluate Stewart's decision.

Stewart then made a demand upon Cross Country for reimbursement. Cross Country, viewing itself as bound by contractual requirements to Stewart, provided the reimbursement. Again, the contract requiring such reimbursement by Cross Country was not in the record – an important lapse.

Cross Country then sued Hill for misrepresentation and unjust enrichment. The trial court dismissed the misrepresentation claims but granted summary judgment to Cross Country in unjust enrichment.

On appeal, *held: Reversed and remanded*, but with some hope. The plaintiff escrow agent did not supply a critical piece of evidence, so the Court of Appeals reversed summary judgment in its favor. Nevertheless, the analysis of the decision favors the escrow agent's position. In essence, the court rejected Hill's arguments that she could not have been unjustly enriched by Cross Country, because Cross Country was just an intermediary and had no financial stake in the closing. It also rejected Cross Country's argument that it had benefitted Hill by drawing the settlement check on its own account.

The court, rather, focused on what happened later, when Stewart Title paid the loan to Provident, and Cross Country reimbursed Stewart for such payment. It invoked the notion that unjust enrichment occurs when one pays a debt more properly chargeable to another. Although Hill likely wasn't personally liable on the debt, she probably was liable under her deed warranty, if for no other reason. Also, she likely was liable to Stewart on the basis of her affidavit concerning clear title.

The court noted that it really didn't matter whether Hill in fact knew or misrepresented that the Provident loan was still outstanding, since (as explained above) she'd be liable to Stewart or the Buyer whether she actually knew or not. (Here's where the court commented that in fact she had to have been aware of a loan on which she'd been making installment payments for over a year.)

Nothing is clearer, however, than that a mere volunteer or officious intermeddler do not have the right to claim unjust enrichment when they pay the debt of another. For word mavens, the court then went into an extended discussion of the meaning of the terms "mere volunteer" and "officious intermeddler" – both beloved of mortgage professors. It concluded that, although these terms sometimes appear independently, they both have the same meaning. It also talked a lot about subrogation cases involving these terms, and concluded that it is necessary for clarity of Maryland law that the terms have the same meaning in the subrogation context as in the unjust enrichment context.

Hill argued strenuously that to qualify for an unjust enrichment claim Cross Country had to show that Stewart had a true obligation to pay the debt and that Cross Country had a true obligation to pay Stewart. Hill claimed that she was entitled to prove at trial that Stewart should have raised an estoppel defense against Provident and that Cross Country should have refused to pay Stewart when Stewart did not raise such a defense.

The court demurred. Its adoption of the position of the Restatement of Servitudes probably sums things up, although there is more discussion in the opinion (note that the same concept applies to subrogation as well as unjust enrichment claims):

"[A] plaintiff may recover for payment or payments to a third party as long as the plaintiff was not officious in making such payment or payments . . . . Generally a plaintiff is not officious when he or she acts under a legal compulsion or duty, acts under a legally cognizable moral duty, acts to protect his or her own property interests, acts at the request of the defendant, or acts pursuant to a reasonable or justifiable mistake as to any of the aforementioned categories."

As indicated, since Cross Country provided no evidence of any contract obligation to Stewart to reimburse Stewart other than the bald assertion that such obligation existed, there was inadequate basis for summary judgment and the court therefore reversed the grant of summary judgment.

Helpfully, however, the court goes on to assume that Cross Country eventually would produce such a contract and it would show that it had an obligation to reimburse Stewart if Stewart were not, in turn a "mere volunteer."

But the court states that, as it defined mere volunteer, even if Stewart did have an equitable defense, Cross Country still would be entitled to unjust enrichment if Cross Country reasonably believed that Stewart was not a mere volunteer. It appears that there is a "double reasonableness" filter here. Stewart was not a volunteer if it reasonably believed that it could not raise an equitable estoppel claim here, and Cross Country was not a mere volunteer in paying Stewart if it reasonably believed that Stewart was reasonable in Stewart's belief. Obviously one of the parties is going to have to summon the entire philosophy faculty at the University of Maryland to sort this one out.

Finally, we hope the reader is still awake – we get to the final question. Did the court's ruling that Cross Country might have an unjust enrichment claim deprive Hill of an equitable estoppel defense Hill might herself have been able to raise if Stewart and Cross Country had made a subrogation claim through the mortgage rights of Provident rather than an unjust enrichment claim? Not at all, says the court. The equitable estoppel claim didn't belong to her – it belonged, if at all, to Stewart and Cross Country. She got the money that should have gone to Provident. She did not suffer a detriment as a consequence of its alleged negligence in explaining the payoff. The court states that Hill raised no legal support for the assertion that a seller of real estate is allowed to assert equitable estoppel against a mortgagee who gives an incorrect payoff amount.

Comment: What a rich analytic treasure trove for mortgage law lovers. As to the rest of you, go back to sleep. The editor thinks the case is well reasoned and on the nose, despite the complexity of the "double reasonableness" conundrum. The trial court probably will be able to sort that one out.

GUARANTEES; CONTRIBUTION; LETTERS OF CREDIT: Party obtaining letter of credit to provide partial guarantee for real estate loan may not assert equitable contribution or subrogation claims against other loan guarantors. ***Morgan Creek Residential v Kemp 153 CA4th 675, 63 CR3d 232 (2007),*** discussed under the heading: "Letters of Credit; Co-guarantors; Contribution."

HOUSING; DISCRIMINATION; FINANCIAL BASED DISCRIMINATION: Provision of alternative housing voucher program (the "AHVP") lease giving tenant right to terminate occupancy on one month's notice a "requirement" of the AHVP program, and landlord cannot reject provision or tenant for financial reasons without running afoul of the housing antidiscrimination law, which prohibits discrimination against tenants who receive public housing subsidies either "because the individual is such a recipient," or "because of any requirement" of the subsidy program despite a lack of animus on the part of the agent. ***DiLiddo v Oxford Street Realty, Inc., 876 N.E.2d 421 (Mass., 2007)***.

The Supreme Judicial Court of Massachusetts held that the lease termination provision at issue is a requirement of the AHVP based on its statutory interpretation that the AHVP has broad grant of power to accomplish its mission of providing temporary transitional housing to needy tenants. Crucial to its finding was the aftermath to the earlier, similar, case of *Attorney Gen. v. Brown,* 511 N.E.2d 1103 (Mass. 1987) in which the court sustained the objections of a landlord to a form "Section 8" housing program lease. After *Brown*, the Massachusetts legislature amended the relevant law to widen the scope of the anti-discrimination law from preventing landlord from discriminating "*solely* because the individual is [a recipient of benefits]" to preventing discrimination "because of any requirement" of the housing program for the purpose of eliminating the loophole that Brown provided landlords.

In addition, the court rejected the Defendants' claim that they should not be held responsible because they lacked animus and because they acted on the advice of council. The court rejected both defenses because the statute requires neither a showing of either animus nor a willful or intentional mens rea. The Court reverse the denial of the Plaintiff's motion for summary judgment, vacated the order granting summary judgment to the defendants, and remanded the case to the Superior Court.

HOUSING; SECTION 8; CHANGES IN STATUS: Landlord breaches Tenant's right to quiet enjoyment by changing Tenant's Section 8 status to Section 236, permitting Defendant to recover damages for emotional distress suffered as a result of the breach. ***Homesavers Council of Greenfield Gardens, Inc. v. Sanchez, 70 Mass. App. Ct. 453 (2007)***, discussed under the heading: "Landlord/tenant; Public Housing; Section 8."

INSURANCE; LANDLORD/TENANT; SUBROGATION; IMPLIED WAIVER OF SUBROGATION: In the absence of an express contractual agreement to the contrary, a tenant will be deemed an implied co-insured under a landlord's insurance policy, thereby prohibiting the insurer from seeking subrogation to the insured landlord's claims against the tenant to recover damages for damages to the landlord's property caused by the tenant. ***Dattel Family Limited Partnership v. Wintz, ___ S.W.3d ___ (Ten. Ct. App. 2007)***, discussed under the heading: "Landlord/Tenant; Insurance; Waiver of Subrogation; Implied Waivers."

LANDLORD/TENANT; ASSIGNMENTS AND SUBLETS; LANDLORD'S CONSENT: Where landlord has a right to consent to any proposed assignment or sublet, and tenant transfers leasehold without landlord's consent, landlord still must establish that such transfer is a "material breach" in order to terminate the lease on that basis. ***Collins v. McKinney, 871 N.E.2d 363 (Ind. Ct. App. 2007)***.

Collins entered into a five year lease agreement with McKinney ("McKinney"). The lease included a restriction that McKinney could not sublease the premises without Collins' prior written consent. The Lease provided expressly that McKinney would remain liable on the lease regardless of whether Landlord consented to any assignment or sublet (which would likely have been the legal result anyway).

On the same day the Lease was entered into, with Collins' consent, McKinney entered into a sublease with another party ("Sublessee"). The Sublease stated specifically that it was subject to the terms of the Master Lease. Later, Sublessee entered into an asset purchase agreement with Glenbrook which provided that Glenbrook would take possession of the property and pay rent to McKinney for a year prior to the close of the asset purchase agreement itself. Collins never gave consent to the Glenbrook's entering the property, although McKinney did approve the arrangement. Collins specifically requested that McKinney eject Glenbrook. She sent a thirty day notice of default prior to termination of the lease.

To forestall termination of the lease, McKinney sought declaratory judgment that Sublessee could assign his interest to Glenbrook without Collins' consent. Collins counterclaimed that McKinney was in breach of the Lease because Glenbrook was in possession of the property without Collins' consent. The trial court granted a motion for directed verdict in favor of McKinney on the basis that regardless of whether there was a breach of the covenant, Collins could not terminate the lease because Collins could not demonstrate any damages. The contracted for rent in under the lease had been paid in full and McKinney remained liable into the future for such rent.

The Court of Appeals reversed this holding, but instead of finding that Collins was entitled to a directed verdict, remanded for a trial on the facts as to whether the transfer of possession to Glenbrook was a sublease or assignment and whether it in fact constituted a material breach.

The court noted that the "purpose of a covenant against assigning and subletting in a lease is to reserve to the lessor the right to say who should occupy the premises" and that by not obtaining Collins' approval of Glenbrook, McKinney's actions "deprived Collins of the [contractual] right to say who should occupy the property." Because Collins was deprived of her contractual right to choose who lives on her property, a jury could find that she had been damaged. Collins had alleged in her brief that she might be exposed to environmental liability or premises liability as a consequence of the activities of whoever was on the premises, and consequently had a right to demand the opportunity to review the proposed transfer.

The court cited the Restatement of Contracts on the question of whether a given breach of contract is "material," and summarized the five factors set forth in the Restatement. They include the extent of injury to the injured party, the extent to which adequate compensation can be made, the likelihood that the party in breach will breach again, and the possibility that the defaulting party will suffer a forfeiture, and the extent to which the behavior of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing. Because a lessor does not have to show monetary loss to show damages where a lessee violates a lease covenant, the court reversed the trial court on this point.

The court of appeals stated that McKinney was required to obtain Collins' consent before any assignment or sublease of the sublease. McKinney argued that while Collins had to consent to the original sublease, the sublessee could then do what it wished with its interest. The court of appeals quickly dismissed McKinney's argument, asking rhetorically, "if Collins had veto power over the original Sublease, then why would she not have the same veto power over a sublease or assignment of that" original sublease. If the contract is silent, it is assumed that if the lessor retains veto power over a sublessee, the lessor retains such power over any further subletting as well.

Comment 1: The editor is dismayed that the court viewed the materiality of the breach to be a question for a jury. Astonishingly, the court fails to cite or discuss *First Federal Savings Bank v. Key Markets,* 559 N.E.2d 600 (Ind. 1990), which holds categorically that where the landlord has reserved a consent right, the landlord has unequivocal right to determine who will occupy the premises. Although it might be a jury issue whether the transfer through an asset purchase agreement was in fact an assignment or sublease (in the view of the editor it was as a matter of law), and although there might be some issue as to whether McKinney could cure (but how could cure be effective now, years later?), it is difficult for the court to fathom how the court could view a tenant's usurpation of the landlord's right to approve who will control the premises to be anything other than "material" as a matter of law. The case is remarkably poorly reasoned from the standpoint of standard landlord/tenant law, which *Key Markets* made plain is the law of Indiana on the issue of lease transfers. As is still the case in the majority of American jurisdictions, a landlord with a consent right has no implied duty of good faith and fair dealing in Indiana.

Comment 2: Although the court might be saying that McKinney should have the right to restore the possession back to the original sublessee and through out the interloping Glenbrook and thus avoid forfeiture, the editor doesn't read the opinion that way. Others are free to argue differently.

LANDLORD/TENANT; ASSIGNMENTS AND SUBLETS; LANDLORD'S CONSENT: "Asset transfer agreement" may be an equitable sublet or assignment of leased business property and require consent of landlord under consent clause in master lease. ***Collins v. McKinney, 871 N.E.2d 363 (Ind. Ct. App. 2007)***. Another aspect of the case and the basic facts are discussed in another item under this same heading.

A sublessee of an auto dealership property entered into an "Asset Purchase Agreement" with another dealership, Glenbrook. The Agreement was signed in July of 2004 but would not close until February 2005, at which time the sublessee would "assign its interest in the Sublease" to Glenbrook. In the meantime, the Agreement provided that Glenbrook would take possession of the property and pay rent directly to the sublandlord.

The Master Lease gave the Landlord the right to review and approve any proposed subleases or assignments, and the Landlord objected to the transfer to Glenbrook. Prior to closing of the Asset Purchase Agreement, she threatened to terminate the lease and the Master Tenant brought suit for declaratory relief alleging, in part, that the Asset Purchase Agreement did not constitute a prohibited assignment or sublease. The trial court directed a verdict against the Landlord.

The appeals court here confronted the issue of whether the transfer breached the lease. The lower court had assumed that there was a breach, but held the breach to be immaterial and not supportive of a lease termination. The appeals court reversed the trial court's finding that the alleged breach was not material as a matter of law, and thus had to reach the question of whether, as a matter of law, there was no breach.

Tenant argued that the arrangement prior to closing of the Asset Purchase Agreement was nothing more than a management agreement, and that the original sublease (to which the Landlord had consented) remained in effect. The court held that at least the Landlord had presented sufficient evidence for a jury issue. In addition to the payment of rent, there was evidence that Glenbrook in fact was selling a different line of cars than the first sublessee had sold, and was effectively in control of the leased premises. In addition, Glenbrook apparently did take possession of a small additional parking lot, a separate lease parcel, and was parking cars there.

Comment 1: The tenant got very lucky to have only a remand for jury trial, which will load up the Landlord with sufficient cost and uncertainty to produce a settlement. Although indeed the sublease would not be fully and formally assigned until after the Asset Purchase Agreement was completed, it does appear that if Glenbrook had sufficient control over the assets to pay the bills, including the rent, and was selling cars other than those sold by the original sublessee, there was a transfer of possession, which is the essence of a sublease, if not an assignment.

Note: There is a remarkable discussion of a prior Indiana case in which a court had held that a sublease of only a portion of the premises is not a breach of a provision prohibiting sublease of the premises. *Drake v. Eggleston*, 108 N.E. 2d 67 (Ind. App. 67) (1952). The court got around *Drake* because the lease here prohibited assigning or subleasing "all or any part" of the premises without landlord's consent. But cases out there like *Drake* obviously provide a caution to landlord's counsel.

LANDLORD-TENANT; COMMERCIAL; SHOPPING CENTERS: Federal court rejects various claims of antitrust violations in "going dark aggressively" case. ***Delco LLC v. Giant of Maryland, LLC, 2007 WL 3307018 (U.S. Dist. Ct. D. N.J. 2007).***

A shopping center owner and a customer of a tenant supermarket sued the supermarket and a food cooperative for alleged antitrust violations. A proposed acquisition of the supermarket tenant by the cooperative would have closed the supermarket's store. The cooperative was planning to keep the leased space vacant while continuing to pay full rent. The landlord and the consumer filed a motion for preliminary injunction and for a temporary restraining order to enjoin the contracting parties from closing the supermarket. They asked the court to invalidate a provision in the supermarket's lease that would have prevented other supermarkets from opening in the shopping center. The landlord claimed that this alleged antitrust violation would result in its loss of the economic advantage of having a continuing supermarket operation, and cause a potential loss of tenants, customers, and income.

The defendants responded that the acquisition of the supermarket was part of an overall strategy by the supermarket chain to terminate its activity in this region of the state. In fact, defendants claimed that the supermarket had required that this store be included in the acquisition, even though it was a heavy money loser.

The Court denied preliminary injunctive relief to both the landlord and its tenant. It ruled that there was insufficient evidence of *per se* monopolization or other Sherman Act violations, at least at the summary judgment level. There were sufficient other explanations for the conduct of the cooperative and the other supermarket to deflect charges of conspiracy in restrain of trade or division of the market.

The case has an interesting summary of two credentialed economists discussing monopolization in the context of supermarket locations. One economist defined the relevant market as that of supermarket-type stores, and on that basis demonstrated that the cooperative had established a sufficient market presence with this acquisition that it would be able to increase prices without driving consumers to other supermarkets, as the market area was contained and there was no competition within it. The other economist accepted the basic analysis, but claimed that the relevant market did not just encompass supermarkets, but included both large and smaller grocery retailers, including, for instance Wal Mart. When these retailers were included in the market, it was clear that there was no monopolization, as there were several such outlets within the market area and, the economist explained, any price increase by the cooperative would drive customers to these other stores. Plaintiffs insisted that a market defined only by supermarket style food retailers was appropriate.

Going forward to further proceedings, the court held that the landlord lacked standing to bring an antitrust action because its alleged injury was merely an incidental by-product of alleged anti- competitive conduct and not the direct result of the alleged scheme. It noted that the landlord was neither a customer nor a competitor in the market in which trade was allegedly restrained. Instead, it was only a supplier providing retail space to market participants. It held that suppliers to direct market participants typically cannot seek recovery under antitrust laws because their injuries are too secondary and indirect to be considered antitrust injuries.

The Court found, however, that the consumer had standing to sue because of his claim that he shopped regularly at the supermarket and alleged that, as a result of its closure, he would be denied the benefits of free competition and face higher prices and limited consumer choice. The consumer was not "disqualified" because he was also construction manager of the plaintiff landlord. On the other hand, it found that while he had standing to bring an action for injunctive relief, he was not entitled to an award for treble damages because such an award requires a showing of an actual injury in addition to a showing of threatened loss or damage.

Comment 1: The court seemed to buy the larger market definition, and this case doesn't look like its going very far. For another case finding that a shopping center developer lacks standing in a case like this one, this time at the Federal Circuit Court level, see *Serfecz v. Jewel Food Stores*, 67 F.3d 591 (7th Cir. 1995) (the DIRT DD for 2/15/96).

Comment 2: As added ballast, the court commented that it didn't appear that the Landlord would be able to show substantial injury anyway. It anticipated that there would conceivably be a vacancy when it leased to the supermarket with an exclusive clause protected the space but no continuous operation clause and a right to sublet. Although there is some merit to this notion, the editor notes that there is at least one case holding that a tenant with a right to sublet nevertheless has a duty sounding in good faith and fair dealing to sublet to a tenant that will generate comparable percentage rents. *Olympus Hills Shopping Center, Ltd. v. Smith's Food & Drug Centers, Inc.*, 889 P.2d 445 (Utah App. 1994) (The DIRT DD for 5/25/95). But compare *Oakwood Village, LLC, v. Abertsons Inc.*, 104 P.3d 1226 (Utah 2004) (the DIRT DD for 3/10/05), a subsequent Utah Supreme Court case that is more appreciative of the tenant's position generally.

Comment 3: As to the claim that the cooperative might engage in monopolization by enforcing the exclusive use clause while leaving its store vacant, at least one case holds that a tenant cannot use the "catbird seat" exclusive in that way. *Tippecanoe Assocs. II, LLP v. Kimco Lafayette 671, Inc.*, 829 N.E.2d 512 (Ind. 2005) (the DIRT DD for 2/2/06). ("Exclusive" covenant in commercial lease is unenforceable where tenant has no interest in shopping center other than prohibiting competition.)

LANDLORD/TENANT; EXCULPATORY CLAUSE; GOOD FAITH AND FAIR DEALING: Even in lease between major commercial parties, a clause limiting remedies to equitable relief (excluding damages) for landlord's failure to review promptly proposed tenant improvement plans will not protect landlord from a damages claim based upon breach of good faith and fair dealing in "extortionate" demand for unwarranted fee to carry out the review. ***Bank of America Securities, LLC, v. Solow Building Co. II, LLC, 847 N.Y.S.2d 49 (12/4/07)***.

A lease for a substantial amount of space in a commercial office building in downtown Manhattan provided that the landlord had the right to review and approve in advance tenant's substantial proposed tenant improvements. The lease provided that landlord could not unreasonably withhold its consent to proposed. It further provided that Landlord would approve or disapprove proposed alteration plans within 10 business days and that, upon substantial completion of the work, could recover its "actual out-of-pocket expenses reasonably incurred in connection with such Alterations."

The lease contained a relatively unusual clause limiting landlord's liability if landlord failed to approve the proposed improvements promptly or reasonably:

"Tenant hereby waives any claim against Landlord which Tenant may have based upon any assertion that Landlord has unreasonably withheld or unreasonably delayed any consent requested by Tenant, and Tenant agrees that its sole remedy shall be an action or proceeding to enforce any related provision or for specific performance, injunction or declaratory judgment or an arbitration proceeding."

Tenant has carried out over $215 million in tenant improvements. The landlord demanded a $6 million fee (basically 3%) to review tenant improvements. Tenant argued, not unreasonably, that this fee far exceeded "landlord's out of pocket expenses reasonably incurred" in reviewing the proposals. Tenant refused to pay, and Landlord in response refused to consider any further proposed improvements.

Landlord took the position that the refusal to pay was a breach justifying termination of the lease and refused to consider any further improvement proposals until Tenant paid the demanded fee.

Tenant sued for declaratory relief and for damages it suffered by being unable to carry out any tenant improvements after the landlord refused to review any more proposed plans. The sole issue covered by this appeal is the trial court's granting summary judgment on the damages claim.

The Appellate Division panel reversed 3-2, with "hot" opinions on both sides. The majority ruled that Tenant could go to trial to show that Landlord's actions were in bad faith. The dissent said that Landlord ought to be protected by the clause because, even if the demand for the $6 million fee had no basis in the lease, it was simply an effort to get money, not an exercise of bad faith, and because the clause gave tenant an adequate basis to address landlord's actions.

The majority opinion stated that, on the basis of public policy, courts will not enforce exculpatory clauses when the conduct of the party seeking protection of the clause is willful. It grounded its opinion on precedent dealing with exculpatory clauses for negligence claims, noting that such clauses have not avoided liability where defendant's conduct was "willful" or "grossly negligent." The court viewed the Landlord's conduct here as "willful." Although the Tenant, in fact, had not alleged any tort theory, but only a breach of contract, and did not specifically allege a breach of the implied duty of good faith and fair dealing, the majority opinion supplied that claim for the Tenant, stating that the use of the terms "malice" or "willful" is not material to a plaintiff's claim when the facts as alleged show that the defendant acted in bad faith.

The majority's response to the dissent's claim that Landlord's conduct should not enjoy the protection of the exculpatory clause was to call the dissent's analysis "illogical, contrary to law, and predicated upon unwarranted findings of fact."

The dissent, citing prior New York authority, argued that to find that an exculpatory clause will not protect a breach of contract deemed by the court to be "willful" basically reads the clause right out of the contract. Breaches of contract are rarely accidental. In the precedent case, the Court of Appeals had permitted a defendant to avoid liability under such a clause when it abandoned a software contract – in direct breach of its contract obligations. The majority stated that defendant's failure to meet its contractual obligations in the precedent case "was an action squarely grounded in the defendant's contractual rights." Here, however, the court stated that the Landlord's "misconduct extends well beyond a simple breach of the parties' agreement, seeking to impose upon Tenant a new contractual burden unrelated to the lease." It characterized the Landlord's behavior as a "classic case of economic duress" (another characterization not made by the Tenant in its pleadings.)

As indicated, the dissent poo-pooed the notion that Bank of America – the tenant, was intimidated by the Landlord's hardball ploy.

"[T]o the extent that, as [Tenant] maintains, the review fee is without a plausible basis in the lease, [Landlord's] demand for it is not likely to have intimidated a sophisticated party like [Tenant.] Indeed . . . a demand so unsupported by the lease would instill derision rather than fear. An obvious popgun is not much of a threat or the weapon of choice for extortionists."

The dissent also notes that the lease obligated the Landlord to agree to expedited arbitration if, in the Tenant's view the Landlord's failure to consent to its proposals was "unreasonable." In this connection, the lease reiterates that the arbitrator's award cannot include damages.

Comment 1: The dissent has it right on the policy. Whether it is right on the precedent is for New York lawyers to resolve – but it appears to be right there also. Sophisticated parties ought to be able to limit remedies for breach of contract. This is a different question from limiting tort remedies. But when the contract language specifically targets the contractual duty in question, how can there be any argument as to what the parties intend? Remember that we are not talking here about the claimed breach of contract, but only about the Landlord's refusal to continue to review and approve tenant improvement proposals unless it receives a three percent fee. This is not tortious. Not even the majority really contends otherwise.

Comment 2: Some might argue that at some point a party's conduct is so "egregious" that any contractual waiver ought to go out the window. But this gets us into the question of "just how egregious?" These were big boys. Tenant didn't have to waive its right to recover. Contrary to the majority's contention, it wasn't faced with years of litigation. It had an expedited arbitration remedy. Further, undoubtedly an appropriate equitable remedy could be devised – appointment of some kind of receivership, for instance, to perform landlord's functions when landlord absolutely refuses. Or there could even be declaratory relief that tenant need no longer seek landlord's approval because of demonstrated failure by landlord to conduct reasonable and timely review.

Comment 3: As to the alleged breach of the separate covenant of good faith and fair dealing: good faith duties do not and should not exist when the parties clearly contractually confer upon one another specific contract privileges – the "right to be unreasonable." If we don't abide by that standard, we invite the courts into retroactive review of every business decision that results in an unappealing loss for the plaintiff.

Things often look much more unreasonable in retrospect. Further, sophisticated business parties should be permitted to take hard positions in business. The best defense is a hard position back.

LANDLORD/TENANT; INSURANCE; WAIVER OF SUBROGATION; IMPLIED WAIVERS: In the absence of an express contractual agreement to the contrary, a tenant will be deemed an implied co-insured under a landlord's insurance policy, thereby prohibiting the insurer from applying the doctrine of subrogation against the tenant to recover damages. ***Dattel Family Limited Partnership v. Wintz, ___ S.W.3d ___ (Ten. Ct. App. 2007).***

Dattel owned a multi-family apartment complex in Memphis and obtained a fire insurance policy from Travelers. Dattel was the only named insured under the policy. On July 25, 2003, a fire occurred at the apartment complex, resulting in damage to Wintz's apartment, which Dattel had leased to her at some time prior to the fire, and to other parts of the apartment structure.

In fulfillment of its obligations under the insurance policy, Travelers paid Dattel $144,575.81. Subsequently, Travelers and Dattel (collectively, "Plaintiffs") filed a lawsuit against Wintz, alleging: (1) negligence, due to the fact that Wintz allegedly discarded matches that had not been completely extinguished into a wastebasket; and (2) breach of contract, based on the fact that the fire damage made future performance under the lease impossible, giving Dattel the right to terminate the lease and triggering a contractual duty of Wintz to return the apartment in good condition or reimburse Dattel (which she could not do). Wintz denied those allegations, and in her motion for summary judgment, asserted that she was an implied co-insured under the liability insurance policy between the Plaintiffs. As such, Wintz argued that Travelers had no right of subrogation, and therefore it could not maintain an action against Wintz for damages to the building.

The trial court granted Wintz's motion, holding that in the absence of a contrary provision in the lease, Wintz was an implied co-insured under the insurance contract between the Plaintiffs, which precluded Travelers from asserting a subrogation claim against Wintz. On appeal, the Tennessee Court of Appeals addressed this sole issue to determine whether the trial court had erred in reaching that conclusion.

The court began by examining the terms of the lease between Dattel and Wintz, in an attempt to ascertain the parties' intent. While the lease explicitly stated that Wintz was expected to obtain renter's insurance to cover her personal property, it was silent on whether she was obligated to obtain insurance for the apartment building. In addition, the lease provided that Wintz would be held liable for any damage done to her apartment during the tenancy, as well as damage to the building's common areas. Despite this language that Wintz would be responsible for damage to the premises, the lease did not state whether Wintz would be a co-insured. Because Wintz was not explicitly listed as a co-insured, Traveler's sought to apply the doctrine of subrogation to recover from Wintz amounts paid to Dattel under the policy.

The court began its analysis by discussing subrogation generally, including its purpose and policy. As a part of this discussion, the court noted instances where subrogation is not appropriate; namely, the right cannot arise in favor of an insurer against its own insured. Therefore, if a tenant is deemed a co-insured under a landlord's policy, "the insurance carrier would be barred from bringing a subrogation action against the tenant to recover for damages to the landlord's insured premises." Further, "a court may consider a tenant to be an 'implied co-insured' under a landlord's insurance policy if it finds that the landlord's insurance coverage was intended for the mutual benefit of the landlord and the tenant, even if the tenant is not a named co-insured." While the Tennessee Supreme Court affirmed a Tennessee Court of Appeals' decision in a prior case involving this issue, it did so based on ambiguity in the lease agreement specific to the case and without directly addressing the issue of "whether the tenant in that case would be deemed an implied co-insured under the landlord's insurance policy." Therefore, after its introductory analysis on subrogation, the court addressed the issue anew by examining the merits of three general approaches used in other jurisdictions when analyzing this issue.

First, in some jurisdictions, courts hold that, "absent a clearly expressed agreement to the contrary, the tenant is presumed to be a co-insured on the landlord's insurance policy, and therefore the landlord's insurance carrier has no rights of subrogation against the negligent tenant."

This approach is frequently referred to as the "*Sutton* approach" (referencing an Oklahoma appellate case), and as the court notes, appears to be the "modern trend" favored by legal commentators." Second, in a minority of jurisdictions, courts hold that "absent a clear contractual expression to the contrary, the insurance carrier will be permitted to sue a tenant in subrogation." This approach is known as the "Anti-Sutton approach." Finally, in order to avoid a per se rule, a slight majority of jurisdictions apply an intermediate approach, holding that "the applicability of the doctrine of subrogation should be assessed on a case-by-case basis and governed by the intent and reasonable expectations of the parties under the facts of the given case."

After an in-depth discussion of each approach, the court rejected the "anti-*Sutton*" and intermediate approaches, choosing instead to apply the *Sutton* approach. With respect to the anti-*Sutton* approach, the court found that while it is consistent with the general principle that a party should be liable for its negligent acts, this approach "is not consonant with the realities of residential leasing or expectations that would be reasonable for the parties." In addition, it promotes economic waste by requiring both landlord and tenant to obtain duplicate insurance. With respect to the middle approach, the court found the approach too uncertain, noting that it would likely result in more litigation. In contrast, the court was persuaded by the reasoning underlying the Sutton approach, which (1) corresponds with the reasonable expectations of the parties; (2) is in accord with the commercial realities involved in insuring residential lease properties; (3) comports with sound economic policy; and (4) provides greater certainty.

Applying the *Sutton* approach, the court ultimately held that in the absence of an express agreement to the contrary, Wintz was deemed an implied co-insured under Dattel's insurance policy with Traveler's, and therefore subrogation would not be permitted.

Comment 1: The editor has exhaustively (he hopes) analyzed all the cases on this issue in Friedman on Leases (Randolph Edition), Sec. 9.11. He agrees that the court correctly identified the *Sutton* rule as the developing consensus, and that the court properly applied it here. There is much force to the argument that the tenant's dollars are being used to pay for the insurance, and the insurer is faced with no significantly greater risk when insuring against tenant-caused accidents as opposed to landlord-caused and unknown case accidents.

Comment 2: Note that the Editor's discussion in *Freidman* includes discussion of both residential lease cases, such as the instant case and commercial lease cases. *Sutton* involved a residential tenancy and in fact appeared to limit its holding to that context.

Although many commercial lease cases involve express waivers of subrogation favoring both landlords and tenants, where this is not the case, many of the policy reasons behind the *Sutton* rule would appear to apply as well to commercial leases.

Nevertheless, in the case of commercial leases, courts might be more inclined to follow what the court here called the "intermediate" rule, and to study the contract to see if some agreement by the parties suggests that the parties in fact intended some different result. Under the "intermediate" cases, language specifically stating that the tenant will be liable for negligence is sometimes held to negate any inference that a waiver of subrogation was intended.

LANDLORD/TENANT; LANDLORD DUTIES; HOLDOVERS: New tenant may sue old tenant who holds over for tortious interference with the new tenant's contract rights under the new lease. ***Havana Central v. Lunney's Pub, 2007 Westlaw 4533126 (N.Y.A.D. 12/27/07).***

Lunney's operated a pub in the Times Square neighborhood. Lunney's knew that its lease was expiring and that the landlord had located a new tenant. It was angling to preserve customer good will by arranging to locate to a nearby location. Perhaps also it was trying to induce the landlord to relet to it by causing problems with the new tenant. In any event, although Lunney's knew nine months out that its lease was expiring and that Havana, the new tenant, was moving in, Lunney's didn't vacate at lease end, leaving Havana without a business premises in the hot end of the year holiday period.

Havana brought a lawsuit against Lunneys for tortious interference with its economic opportunity when Lunny's allegedly induced the landlord to fail to perform its contract obligation to deliver the premises on time, and also for tortious interference with prospective economic advantage. Havana alleged that it lost a lot of business opportunities as a consequence of Lunney's failure to move out.

The trial court gave summary judgment to Lunney's and the appellate division here reversed on the tortious inducement count but affirmed the tortious interference count. There was a strong dissenting opinion on the tortious inducement claim, and the case is a good read.

An important element of the case was that the Havana lease contained a waiver of damages clause concerning holdover tenants, apparently common in New York:

"If Owner is unable to give possession of the demised premises on the date of the commencement of the term hereof, because of the holding-over or retention of possession of any tenant . . . or if Owner has not completed any work required to be performed by Owner, or for any other reason, Owner shall not be subject to any liability for failure to give possession on said date."

Lunney's argued that it could not be held liable for inducing the landlord to breach by tolerating the holdover when in fact Havana's lease didn't require the landlord to prevent a holdover.

The majority disagreed. It stated that there is no doubt that the landlord's failure to deliver the premises upon holding over was a "material breach" of the lease notwithstanding the fact that there was no damage claim available. Therefore, it reversed summary judgment against Lunney's so that Havana could prove that Lunney's induced landlord to breach landlord's duty.

The dissent stated that the landlord had no duty to provide possession:

"Putting aside the niceties of the pure question of contract law of whether the landlord breached the lease, it strikes me as indisputable that Havana Central had no legally enforceable right against the landlord to possession of the premises on the commencement date whenever the landlord was unable to give possession."

Comment 1: The editor originally was struck by the fact that neither the majority or minority in this case discussed where New York stands on the common law debate as to whether a landlord has an absolute common law duty to provide possession to the tenant at the outset of the lease (English rule – the majority in America) or not (known as the "American Rule" although it is the minority in America.) This issue is discussed in Section 4.2.1 of Friedman on Leasing, Randolph Edition. In fact, Friedman notes that the "American Rule" is also referred to by Friedman as the "New York Rule," so we know what New York common law provided – no duty.

But Friedman reports that result was changed by statue in New York – 233-a of the New York Real Property Law.

"In the absence of an express provision to the contrary, there shall be implied in every lease of real property a condition that the lessor will deliver possession at the beginning of the term. In the event of breach of such implied condition the lessee shall have the right to rescind the lease and to recover the consideration paid. Such right shall not be deemed inconsistent with any right of action he may have to recover damages."

Friedman goes on to say that, as a consequence of the statute, most New York leases contain a waiver protecting the landlord from liability in the event of a holdover. As noted, the plaintiff's lease in *Havana* contained such a waiver of liability.

Comment 2: The dissent's argument, as noted, appears to assume that it is up to the new tenant to throw out the old tenant. As noted above, though, current New York law is exactly the opposite. Consequently, the landlord had a contract duty, as to which, the editor assumes, specific performance was available, to terminate Lunney's possession. In fact, apparently it did do this in the end. Thus, the editor disagrees with the dissent that the landlord had no duty simply because no damages were available.

But the dissent notes that Havana also had a right to collect damages from Lunney for Lunney's wrongful possession. Therefore, it asks, what's the point of this action against Lunney for tortious inducement?

The editor would agree with the dissent if Havana not only had a claim for damages against Lunney for trespass, but also had the same right to a summary possession action to throw Lunney off the premises that the landlord had, together with any right to attorney's fees that landlord had. I assume that the landlord did have the right, both at law and in the lease, to evict Lunney. If it was more advantageous to Havana for the landlord to do this than it would have been for Havana to do it for itself, then it seems to me that it should be able to show that Lunney "induced" landlord to drag its feet on evicting Lunney. This was a summary judgment action, and we don't know what Havana could have proved. Certainly simply showing that Lunney was there when the lease ended would not be enough.

Comment 4: Still, one must ask why the plaintiff viewed the tortious interference tort as all that helpful. Trespass is also a tort, and presumably could also carry a punitive damages claim. Perhaps Havana pursued the case (and the appeal) because of the other prong in its attack – a suit for wrongful interference with prospective economic advantage. Here the majority and dissent agreed – Havana had no such cause of action. Such a suit is available only when the defendant's alleged tortious action was aimed directly at injuring plaintiff. Here there appeared to be other explanations for Lunney's conduct.

LANDLORD/TENANT; RESIDENTIAL; EVICTION PROTECTION: Where a functional residential co-tenant can show that he or she has been continuously in residence and has been a substantial contributor toward the satisfaction of the tenancy's financial obligations he or she is entitled to invoke the provisions of New Jersey's Anti-Eviction Act if his or her contribution was acknowledged and acquiesced by the landlord. ***Maglies v. Estate of Guy, 193 N.J. 108, 936 A.2d 414 (2007)***.

LANDLORD/TENANT; RESIDENTIAL; PUBLIC HOUSING; DISCRIMINATION: Provision of alternative housing voucher program (the "AHVP") lease giving tenant right to terminate occupancy on one month's notice a "requirement" of the AHVP program, and landlord cannot reject provision or tenant for financial reasons without running afoul of the housing antidiscrimination law, which prohibits discrimination against tenants who receive public housing subsidies either "because the individual is such a recipient," or "because of any requirement" of the subsidy program despite a lack of animus on the part of the agent. ***DiLiddo v Oxford Street Realty, Inc., 876 N.E.2d 421 (Mass., 2007)***, discussed under the heading: "Housing; Discrimination; Financial Based Discrimination."

LANDLORD/TENANT; **RESIDENTIAL; PUBLIC HOUSING; SECTION 8:** Landlord breaches Tenant's right to quiet enjoyment by changing Tenant's Section 8 status to Section 236, permitting Defendant to recover damages for emotional distress suffered as a result of the breach. ***Homesavers Council of Greenfield Gardens, Inc. v. Sanchez, 70 Mass. App. Ct. 453 (2007).***

Homesavers Council of Greenfield ("Plaintiff") owned Federally subsidized housing, where Luz Sanchez ("Defendant") lived as a tenant with her two children. She earned $26,135 per year and received a section 8 rental subsidy that lowered her rent forty-nine dollars to $593 per month. Because the subsidy was minimal, Plaintiff transferred the subsidy to another tenant who would benefit more from section 8 and recertified Defendant under the section 236 program without informing Defendant.

A few months later, Defendant took an unpaid leave of absence from her employment for depression and began receiving public assistance, which reduced her income to $8,292. Under section 8, her rent would have been reduced to $147 per month. She sought such reduction and discovered that Plaintiff changed her subsidy to section 236, which remained unaffected by her lowered income.

Plaintiff served Defendant with a notice to quit for nonpayment of rent and commenced eviction proceedings. The trial court determined that Plaintiff wrongfully terminated Defendant's section 8 subsidy and, thus, interfered with Defendant's right to quiet enjoyment. As a result, Defendant suffered emotional distress and the court awarded her $5,000 in damages, which was doubled under G.L. c. 93A.

Plaintiff appealed and argued that Defendant did not meet the factors required to receive an award for intentional infliction of emotional distress. The Appellate Court held that it was irrelevant whether Plaintiff met the factors required for intentional infliction of emotional distress because Plaintiff suffered emotional distress as a consequence of the breach of quiet enjoyment and did not bring a claim for emotional distress as a separate tort. Thus, "negligent conduct, as opposed to willful or reckless behavior, is all that is required for a violation of the quiet enjoyment statute." *Id.* at 458. Interestingly, the court discusses that if the standards for intentional infliction of emotional distress were held to apply to emotional distress as a consequence for the breach of quiet enjoyment, Defendant still would have succeeded. The Appellate Court affirmed the Housing Court's decision and damages awarded.

Comment: This is wildly out of the Editor's area of expertise, but if subsidized housing providers can and do routinely change certifications of their residents (albeit for good reasons – as here) there is a cautionary tale here. The editor is amazed that changes of this sort may legally be carried out without knowledge to the involved resident.

LETTERS OF CREDIT; CO-GUARANTORS; CONTRIBUTION: Party obtaining letter of credit to provide partial guarantee for real estate loan may not assert equitable contribution or subrogation claims against other loan guarantors. ***Morgan Creek Residential v Kemp 153 CA4th 675, 63 CR3d 232 (2007).***

Kemp and Haws, developers of the Morgan Creek Golf Course, sought to induce Lender to provide a $6.5 million loan. They posted partial guaranties that totaled $4.8 million. Lender wanted more security than that, and so the guarantors induced the master developer of the entire Morgan Creek project, MC, to add an unconditional letter of credit for another $1.4 million. This gave Lender a total of $6.2 million in additional security, over and above the deed of trust – enough for the loan to go through. But, thereafter, the filing of some mechanics' liens threw matters into disarray. Lender responded to the situation by drawing down the letter of credit it was holding and using those funds to reduce the loan balance to $4.8 million, roughly what the project was then apparently worth. Because the parties regarded the loan as again in balance, the promoters refinanced a new $4.7 million loan with Citicapital, and the project was back on track.

MC sued Kemp and Haws for equitable contribution and subrogation. The trial court sustained defendants' demurrer without leave to amend.

On appeal: *Held: Affirmed.* Equitable contribution allows for loss sharing among co-obligors that share the same level of liability on the same risk as to the same principal. MC, which put up an unconditional letter of credit, was a markedly different guarantor than Kemp and Haws, who merely gave guaranties. Because liabilities inherent in these two kinds of security were markedly different, there could be no contribution or subrogation.

The court noted that an unconditional letter of credit given to guaranty a debt is not a form of suretyship obligation, in which the surety's liability is secondary to the liability of the principal for that application. The liability of the issuer of a letter of credit is direct and independent of the underlying transaction between the beneficiary and the issuer's customer. It does not derive from the obligations of the obligor of the guaranteed debt. For instance, unless there is fraud, the issuer cannot refuse to pay based on extraneous defenses arising from the underlying transaction. Thus, when Lender called the unconditional letter of credit furnished by MC, neither MC nor the issuing bank could assert any defenses other than fraud to stop Lender from collecting.

A guaranty, such as those given by Kemp and Haws, is a form of suretyship obligation. Kemp and Haws therefore had defenses under CC §2845 to demands by Lender that were not available to MC. The appeals court reasoned that because Kemp and Haws had suretyship defenses available to them, and MC did not, the parties did not share the same level of liability to Lender. Accordingly, MC could not claim contribution against Kemp and Haws.

MC also claimed a right to equitable subrogation to the rights of Lender. But the court held also that this was not a valid claim. California law states that, to qualify for equitable subrogation, the subrogee must have made payment to protect its own interest; the subrogee must not have acted as a volunteer; and the debt must be one for which the subrogee was not primarily liable. In addition, the entire debt must have been paid; and subrogation must not work any injustice to the rights of others.

Although MC likely did not pay as a mere volunteer, it had a problem in that it was primarily liable on the letter of credit. But even allowing that this did not defeat the subrogation claim (since the letter of credit was a secondary obligation, in a sense), and assuming that the requirement that the entire debt be paid was satisfied by payment of the entire letter of credit rather than the total the golf club owed Lender, the court noted that Kemp and Haws were not primarily liable on the Lender's obligation; the golf club was primarily liable. Additionally, Kemp and Haws, as mere guarantors, bargained for limited exposure. In the court's view, to allow Morgan Creek to recover from them would work an injustice to their rights. Using a subrogation theory to obtain apportionment from others who are not primarily liable was inconsistent with the aim of subrogation: to place the burden for loss on the party ultimately liable or responsible for it and by whom it should have been discharged.

Reporter Roger Bernhardt's Comments: It is certainly true that the obligation satisfied by one must have been commonly imposed upon the others: If A is liable for X's liability on a note to Y and B is liable for X's liability to Y for a personal injury, neither A nor B can make the other share any part of whatever particular loss the other one had to cover. Rather, the requirement is that the obligation is a common one, and I have never seen it read to mean such perfect equality as was required here. If A guarantees payment of $40 of X's $100 note and B guarantees payment of $60 of that same note, §1432 expects that any dollar that one of them pays should be shared 40/60 with the other. The issue is whether the creditor could have turned to either of the co-obligors for payment. The facts are not entirely clear in this case, but it looks like the $6.2 million obligation to Lender was represented by a single note, with each dollar of it covered by all of the secondary security posted, thus making for a common, albeit secondary, obligation. The court of appeal thought otherwise; its reason was that all of the security posted by the defendants was in the form of personal guaranties, whereas the security posted by the plaintiff was in the form of a letter of credit. That mattered for the court, since CC §2787 distinctly states that a letter of credit is not a form of suretyship obligation, whereas the same section also no less distinctly merges guaranties into general suretyship obligations. Letters of credit are subject to the "independence" principal-a doctrine that makes the issuer pay even though the true obligor has good defenses; whereas guarantors, although themselves regarded as independent obligors, are not subject to that same exposure. Given that distinction, the MC secondary parties did not qualify as liable under the rules of contribution.

Now, that is a conclusion that would not have occurred to me. If the lender told my client to purchase a letter of credit to further secure a borrower's loan that already was guaranteed by someone else, I probably would have told my client (had I thought of it) that the differences between her letter of credit and the other person's guaranty meant she would be more likely to be called on first, but not that those differences would destroy any right or liability to contribution if only one of them was called on to pay, as this case holds. I would have expected those differences to matter vis a vis the lender, but not vis a vis the borrower or vis a vis the two secondary parties. Had I been really cautious, I would have suggested an agreement between these two secondary parties – to settle all of the details of contribution between them – but not to create a right that would not otherwise exist because of their different levels of liability. But from now on, all of us had better insist on such an agreement. After this decision, who can say, for instance, whether there are contribution rights between two guarantors, one of whom has posted a deed of trust to secure his guaranty and the other had given an unsecured guaranty (or a guaranty secured by personal rather than real property)? Will there still be contribution if one guarantor has waived all defenses and the other has not?

When common liability was the only prerequisite to contribution, it did not matter that the theories or amounts of liability were different, and there was no great need for attorneys to make the agreements say more. But now that the standard is higher and narrower, attorneys should create contractual rights to contribution to fill in these gaps of equitable contribution (and hope that the courts will permit that to be done). Will that be hard to do?

Since, generally, neither party will be able to predict which one will be first called on to pay, it should not be hard to draft an agreement both will accept. It's probably what any two parties under such a veil of ignorance would want in any case: If one pays, the other shares. I would suggest boilerplate language, such as:

"The parties agree that the principle of contribution shall apply to any obligation they share in common in this transaction, notwithstanding the fact that their obligations are determined to be at different levels of liability or otherwise different."

Reporter Dan Schechter's Comment: I disagree. It is true that a bank that issues a letter of credit is not a surety and is not entitled to seek contribution. But the applicant for the letter of credit was certainly a surety: It incurred a contingent obligation (the reimbursement of the issuer of the letter of credit) in support of the primary debtor's obligation to the lender. There is no authority for the idea that an applicant for a standby letter of credit cannot qualify as a surety. Here, the applicant and the guarantors were co-sureties, entitled to contribution. The applicant is as much of a surety as someone who does not assume personal responsibility for the debt but who puts assets at risk in a nonrecourse hypothecation. *See, e.g., Pearl v General Motors Acceptance Corp*. 13 CA4th 1023, 16 CR2d 805 (1993) .

The cases cited by the *Morgan Creek* court were inapposite: They dealt with the rights of letter of credit issuers, rather than the rights of applicants. In fact, although the court placed primary reliance on the California Supreme Court's opinion in *Western Sec. Bank v Superior Court,* 15 Cal 4th 232, 62 Cal Rep 2d 243 (1997) , the court later dismissed one of the applicant's arguments that was based on language in Western Security by noting that "[t]he dispute in Western Security Bank was between the parties to the letter of credit transaction." Exactly! *Western Security* is off point, and the court erred by reading too much into that opinion.

The facts of this case were particularly egregious: The guarantors apparently (1) got the benefit of the applicant's money and then (2) sold the property to themselves with a reduced debt load in a "sweetheart" deal. Although the facts of this case are strange, the underlying issue is of great commercial importance: What rules govern the contribution rights of co-sureties? Does the use of a letter of credit (a common device in large transactions) alter those rules?

Whatever happens in this case, however, I also predict that this problem will not arise very often in the future: From now on, sophisticated letter of credit applicants in this situation will demand express contractual contribution agreements from their co-sureties.

Roger Bernhardt is a Professor at the Golden Gate Law School in San Francisco. His comments, originally appearing in the California CEB Real Property Reporter are excerpted with permission.
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The editor heavily modified and rearranged both Roger's and Dan's stuff, and is responsible for any errors, omissions, or stupidity.

LLCs; PERSONAL LIABILITY OF MEMBER-MANAGER: Illinois appellate court holds that plaintiffs could not establish managing member's personal liability for contractual debts incurred by a limited liability company after its dissolution. ***Puleo v. Topel, 368 Ill. App.3d 63 (2006)***.

This decision involved liability arising out of the contractual activity of an LLC. In this case (acknowledged by the court to be an issue of first impression under the Illinois Limited Liability Act (the "Act")), the court held that the member-manager of an LLC was not personally liable for unpaid debts to independent contractors engaged to perform work after the LLC was involuntarily dissolved for failure to file its 2001 annual report.

The court reasoned that because in 1998 the Illinois legislature removed the provision in Section 10-10 of the Act that allowed a member or manager of an LLC to be held personally liable in the same manner as provided in 805 ILCS 5/3.20 (i.e., for his or her own actions or for the actions of the LLC to same extent as a director or shareholder of a corporation), the Act did not provide for a member or manager's personal liability to a third party for an LLC's debts. The court held that under § 10-10 of the Act a member or manager could only be held personally liable for debts and obligations of the LLC if "(1) a provision to that effect is contained in the articles of organization; and (2) a member so liable has consented in writing to the adoption of the provision or to be bound by the provision (citation omitted)."

The court found that in this case neither of these specific requirements had been alleged or proven by the plaintiffs and therefore, "under the express language of the Act, plaintiffs cannot establish [the LLC member-manager's] personal liability for debts that [the LLC] incurred after its dissolution." Id. at 68.

Interestingly, at the end of its opinion the court states that, "We agree with plaintiffs that the circuit court's ruling does not provide an equitable result. However, the circuit court, like this court, was bound by the statutory language."

Reporter's Comment 1: As this case demonstrates, an LLC may well be a better "shield" from liability to the members and managers of an LLC entity than a corporation (at least in Illinois). However, this was an action brought upon an alleged breach of contract, and it is unsure whether an Illinois court would apply the same principles (and holding) if the case had arisen out of a tort claim instead of a contractual dispute. Also, the case involved interpretation of clear and specific language in the Act that protected LLC member-managers from the types of claims asserted by the plaintiffs. As noted by the court, "we . . . decline plaintiffs' request to ignore the statutory language. When the legislature amended section 10-10 (805 ILCS 180/10-10 (West 2004), it clearly removed the provision that allowed a member or manager of an LLC to be held personally liable in the same manner as provided in section 3.20 of the Business Corporation Act. Thus, the Act does not provide for a member or manager's personal liability to a third party for an LLC's debts and liabilities, and no rule of construction authorizes this court to declare that the legislature did not mean what the plain language of the statute imports" (citation omitted).

Reporter's Comment 2: See also *Wachovia Securities, LLC v. Neuhauser*, 2007 WL 4246894 (U.S. Dist. Ct., N.D. Ill., Nov. 29, 2007). Referring to the Illinois Appellate Court's ruling in *Puleo, supra,* the federal district court in this case rejected the plaintiff's argument that because the LLC was dissolved at the time the sole member-manager opened a trading account, the member-manager could be held personally liable for the LLC's alleged breach of contract as a "member or manager" to the same extent as a director or shareholder under Section 10-10 of the Act and Section 5/3.2 of the Illinois Business Corporation Act. The court held (as in *Puleo*) that the 1998 revision to § 10-10 of the Act did not provide for a member or manager's personal liability to a third party for an LLC's debts; accordingly, the sole member-manager of the LLC could not be held liable for the LLC's debts even though the LLC was dissolved at the time single member-manager opened the account.

Reporter's Comment 3: See generally Lin Hanson, *LLCs and Asset Protection*, 95 ILL. B.J. 662 (2007) (discussing *Albright* and *Puleo* decisions); J. William Callison and Maureen A. Sullivan, Limited Liability Companies: A State-by-State Guide to Law and Practice (Current Through the July 2007 Update), §5:1 Liability of Members (discussing Puleo and other recent cases involving LLC members' claims for protection from personal liability for an LLC's debts, liabilities, and obligations).

Reporter's Comment 4: A few years ago, the efficacy of a single-member LLC as an asset-protection vehicle was thrown into doubt by a Colorado bankruptcy-court decision. In *In re Ashley Albright*, 291 B.R. 538 (Bankr. D. Colo. 2003), the debtor, who filed a Chapter 13 bankruptcy petition that was later converted to a Chapter 7 liquidation, was the sole member and manager of a Colorado LLC at the time of the filing. The LLC was not a debtor in bankruptcy. The Chapter 7 trustee contended that because the debtor was the sole member and manager at the time the debtor filed bankruptcy, he now controlled the LLC and could therefore sell the real property owned by the LLC and distribute the net sales proceeds to the bankruptcy estate. The debtor argued that the trustee acted only for the debtor's creditors and at most was entitled to a statutory charging order (against distributions made on account of the debtor's LLC membership interest) and could not assume management of the LLC or sell its property. The court referred to the Colorado LLC statute, under which the debtor's membership interest constituted the personal property of the member. According to the court, "[b]ecause there are no other members in the LLC, the entire membership interest passed to the bankruptcy estate, and the trustee became a 'substituted member.'" The court also stated that, "upon the Debtor's bankruptcy filing, the Trustee now controls, directly or indirectly, all governance of that entity, including decisions regarding liquidation of the entity's assets." The court reasoned that because there were no other members in the LLC, no written unanimous approval of the transfer was necessary, as would be the case under Colorado law if there were other members – no matter how small such other membership interests may be.

Colorado's LLC statute, similar to those in other states, provides that if such unanimous consent is not obtained, the bankruptcy estate is only entitled to receive the bankrupt member's share of the profits or other compensation that the bankrupt member was otherwise entitled to and would not be entitled to any role in the voting or governance of the LLC. However, in a footnote the court stated that this statutory limitation "does not create an asset shelter for clever debtors. To the extent a debtor intends to hinder, delay or defraud creditors through a multi-member LLC with 'peppercorn' co-members, bankruptcy avoidance provisions and fraudulent transfer law would provide creditors or a bankruptcy trustee with recourse." *Id.* at 541 n.9).

The court rejected the debtor's assertion that the trustee should be entitled only to a charging order, holding that a charging order existed only to protect other members of an LLC, and in a single-member LLC there were no non-debtor members to protect. The court ruled that the trustee, as the sole member of the LLC, controlled the LLC and could cause the LLC to sell its property and distribute the net proceeds to the bankruptcy estate, or alternatively the trustee could elect to distribute the LLC's property to the bankruptcy estate, and then liquidate the property himself. However, the court did permit the debtor to make a claim for her post-petition mortgage payments to preserve the real property of the LLC, which was now an asset of the bankruptcy estate.

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

MECHANIC'S LIENS; LEASES: A construction lien against leased property can only be filed if the improvement contract had been authorized in writing by the owner of a fee simple interest in the improved real property; a general provision in a tenant's lease allowing alterations to be made does not satisfy that requirement. ***Cherry Hill Self Storage, LLC v. Racanelli Construction Company, Inc., A-5727-05T5 (N.J. Super. App. Div. 6/18/07) (Unpublished).***

A tenant had a contractor perform real property improvements to its leased property. After making a partial payment to the contractor, the tenant filed for bankruptcy and the contractor, "unable to secure payment from [the tenant], filed a lien claim pursuant to the Construction Lien Law." That law, which generally permits a contractor who improves real property to place a lien on the property if payment is not received, contains a qualification as follows: "If a tenant contracts for improvement of the real property and the contract for improvement has not been authorized in writing by the owner of a fee simple interest in the improved real property, the lien shall attach only to the leasehold interest of the tenant."

The lease included a provision requiring the tenant "to do the work for which it had contracted." The lower court opined that, "There's no question that this lease and the provisions noted were more than adequate to provide the requisite written agreement." The Appellate Division thought otherwise. Basically, it construed the statute by keeping in mind that "the judicial role is to give effect to the legislative intent. First, it looked at the plain language of the statute. In doing so, it noted that the statute "requires written authorization of 'the contract for improvement' pursuant to which the work is done; it does not require written authorization for the tenant to undertake the improvement. Said another way, the statutory reference is to the contract pursuant to which the work is performed and not to the work undertaken pursuant to the contract." Accordingly, because the lease provisions identified by the lower court did not "even reference a particular contract," the Appellate Division held that those provisions could not "constitute authorization for the execution of a specific contract." To aid in its search for legislative intent, the Court looked at a prior version of a similar lien law. That law "permitted a lien on the fee estate when work was done pursuant to a contract where the tenant only if the work 'was [performed] with the written consent of the owner of such land'." To the Court, that language referred to the "landlord's consent to the work rather than the landlord's authorization of a contract." The Court thought that the change in language was significant – it signified "a purposeful alteration in the substance of the law."

Therefore, "[g]iven the legislature's evident intent to require a landlord to authorize a particular contract that may result in a lien upon the landlord's property and the undisputed fact that no such authorization was provided here, [the Court] conclude[d] that the lien was improperly filed."

MORTGAGES; DISCHARGE; FORECLOSURE: Under the merger doctrine, once a final judgment by foreclosure is entered, the mortgage ceases to exist and it is therefore impossible to discharge the mortgage. ***Washington Mutual, FA v. Wroblewski, 396 N.J. Super. 144, 933 A2d. 32 (Ch. Div. 2007).***

A lender sued its borrower to foreclose its mortgage after the borrower defaulted. After the lender received a final judgment of foreclosure, the borrower redeemed. The borrower requested a discharge of mortgage, but the lender argued that the borrower was only entitled to receive a warrant to satisfy the foreclosure judgment. The borrower claimed that it was entitled to a discharge and argued that, without a recorded discharge, title insurers would incur additional investigation expenses to determine that a final judgment by foreclosure was entered and satisfied. The lender argued that based on the merger doctrine, the borrower was only entitled to a warrant to satisfy the judgment and not a discharge of mortgage. Under the merger doctrine, the terms of the mortgage are merged into the final judgment by foreclosure and, as a result, the mortgage is extinguished. Therefore, there is no mortgage to discharge, and the borrower is only entitled to a warrant to satisfy the foreclosure judgment. The lender also claimed that it would be inequitable to require a lender in that situation to issue a discharge of mortgage as opposed to a warrant of satisfaction because it would reward a defaulting borrower that redeems the property at a sheriff's sale and give that borrower the same benefits afforded a borrower that meets its contract obligations by paying its mortgage loan in full.

The Court found that, under the merger doctrine, once a final judgment by foreclosure is entered, the mortgage ceases to exist and it is therefore impossible to discharge. The Court noted that, as a practical matter, the sheriff could record the warrant to satisfy the judgment, which would provide the same notice to title insurers as a recorded discharge of mortgage.

MORTGAGES; FORECLOSURE; CONSTITUTIONAL LAW; DUE PROCESS NOTICE: Combination of mailing first class letter (both to named recipient and to "occupant,") and certified mail letter containing notice of impending foreclosure satisfied Due Process notice requirements under state and federal law, even when court determines that property owner did not in fact receive either notice and certified mail letter was returned "unclaimed." ***Griffin v. Bierman, 2008 Westlaw 360972 (Md. 2/12/08).***

The case is interesting because it involves a Constitutional Due Process analysis of a non-judicial foreclosure process. Typically, with judicial foreclosures, state law provides that the foreclosure be treated as an ordinary lawsuit, with notice provided by service of process. With non-judicial foreclosures, Due Process considerations rarely arise, because no "government action" is involved, and thus the Constitution is not implicated. Thus, what we know about notice requirements for foreclosures and other procedures that involve "government action" but are not lawsuits is somewhat limited. Primarily the authority involves property tax foreclosures, such as in the case of the recent decision in *Jones v. Flowers,* 547 U.S. 161 (2006) (the DIRT DD for 4/27/06). (Supreme Court reinterprets *Mullane* in context of tax foreclosures. County collector must do "something" when it becomes aware that its mailed notice of foreclosure has not been delivered to the property owner. But Court mum on exactly what that "something" is.)

In the instant case, the Maryland non-judicial foreclosure process does involve some governmental involvement, and the parties stipulated that "government action" was involved.

The trustees charged with giving notice of foreclosure complied with the Maryland statute, which requires first class *and* certified mail notice. In fact, the trustees also send a first class mail notice to "occupant" and made the mailings twice, after receiving notification that the original certified mail notice was not claimed. The trustees did not receive any notice that the first class letters did not reach the recipient. The court speculated that if the recipient had received a first class letter from the trustees, it is possible that the recipient would not go to the trouble of claiming a certified letter that arguably contained the same information [but how would the recipient know what the certified letter said – and if she got a first class notice of foreclosure, wouldn't the recipient be much more likely to retrieve the certified letter to see if it contained further information? Ed.]

Of course, *Jones* found the process used in the New York tax foreclosure case to be Constitutionally deficient, but it suggested other forms of notice that might have been adequate, and one of them was what the Maryland statute requires – notice by first class mail combined with notice by certified mail. But the Supreme Court emphasized the governmental burden of complying with complex notice requirements when it was dealing with such a common and repetitive problem as tax delinquency foreclosures. As the Court has stated many times, "mass due process" may require a lower standard than the Constitution might require in individual disputes.

The legal aid group that apparently tried to make a test case out of this dispute argued, apparently, that service of process ought to be the standard of notice in a private home foreclosure.

The mortgagees apparently successfully convinced the court that *Jones* set the standard for a non- judicial foreclosure in Maryland – in other words that such foreclosures were in effect at the same level as tax sale foreclosures. The editor disputes that, but he's not on the court.

Having established that principle, the court had little difficulty analogizing to *Jones* and other tax foreclosure cases. It distinguished other authority suggesting a higher notice standard by characterizing those cases as involving *in personam* proceedings, while the foreclosure proceeding is *in rem.* Again, the editor has difficulty understanding why "fundamental fairness" ought to be different when a homeowner stands to lose ownership of property.

The court noted that established Constitutional principles provide that no one is entitled to receive *actual* notice, but rather to a fundamentally fair attempt to provide notice. As indicated, it drew on precedent from tax foreclosure cases and other *in rem* proceedings to conclude that service of process is not Constitutionally required in a home foreclosure.

Importantly, the court also noted that it was aware that the Maryland legislature was currently reviewing the foreclosure statute and might be considering different statutory notice requirements in the near future. As the policy of the State ought to be carried out by legislative officials, rather than the courts, the court indicated that judicial deference in this case led it to be cautious in dictating a new Constitutional standard under these circumstances.

Comment: The editor perceives no rational basis to differentiate home foreclosures from other proceedings in which a higher standard of notice might be required. *In rem, schmim rem.* Why should this ancient distinction, relevant to jurisdictional issues, be relevant to what is fundamentally fair? Although, of course, a lawsuit can lead to dire and unforeseeable consequences, what can be more dire and unforeseeable than for one to lose one's home without notice?

Further, as the editor has indicated above, he doesn't buy the argument that concerns about overburdening government – present in tax foreclosures – ought to be relevant when a private mortgagee is trying to collect on a private debt.

The argument that the court should step aside when the legislature is working on the problem makes sense, however. But the law the court makes here strikes the editor as more far reaching than might be appropriate in a simple exercise of judicial deference.

MORTGAGES; FORECLOSURE; DEEDS OF TRUST; TRUSTEE'S DUTIES: Trustee under deed of trust merely acts as common agent for trustor and beneficiary and owes no fiduciary obligation to third parties. ***Heritage Oaks Partners v First Am. Title Ins. Co.155 CA4th 339, 66 CR3d 510 (2007).***

This one is worth it just for the story.

Peppertree defaulted on a deed of trust loan from Union Bank. In January 1996, First American Title (First American) conducted a trustee sale on Union Bank's instructions; Union Bank acquired the property by making a credit bid. First American, however, was not the trustee under the deed of trust, as Union Bank had previously substituted itself as the trustee. Heritage Oaks Partners bought foreclosed property from Union Bank in October 1996.

In December 1997, when Peppertree discovered that First American was not the trustee of record incident to the foreclosure sale, it sued Union Bank, First American, and Heritage Oaks, alleging that the foreclosure sale was void. Heritage Oaks incurred over $500,000 in attorney fees defending itself in the litigation. In September 1999, the trial court found in for Peppertree, concluding that the foreclosure sale was void. Peppertree filed a second suit against Heritage Oaks seeking return of the property. Heritage Oaks settled by paying Peppertree Owners $1.4 million and quitclaiming the property to them.

The case continued on appeal against Union Bank and First American, and ultimately the court of appeal reversed, holding that, based on mutual mistake, the trial court should have reformed the deed of trust to permit First American to conduct the foreclosure sale in order to carry out the intent of the parties.

Heritage Oaks then sued First American for equitable indemnity and negligence, claiming that First American breached its duty as trustee under the deed of trust to properly record a substitution of trustee, thereby causing Heritage Oaks to incur attorney fees and other damages. The trial court sustained a demurrer on the equitable indemnity cause of action because First American had not caused any injury to Peppertree Owners; therefore, there was no fault to apportion among the defendants in that action.

The court later granted summary judgment on the claim of negligence, finding that, whether or not First American was negligent, First American had no duty to Heritage Oaks arising out of the foreclosure sale because Heritage Oaks was not a party to the trust deed.

The court of appeal affirmed. It ruled that the trustee under a deed of trust merely acts as a common agent for the trustor and the beneficiary and owes no fiduciary obligations. In order to pursue a claim for equitable indemnity, the defendant must be at least partially at fault.

The court noted that the trustee under a deed of trust is not a true trustee. Its only duties are, on default, to take steps necessary to foreclose the deed of trust or, on satisfaction of the debt, to reconvey the deed of trust. The nonjudicial foreclosure statutes reflect a balance of interests of beneficiaries, trustors, and trustees. They provide quick recovery of amounts due under promissory notes while providing protection against forfeiture of property rights. Trustees are provided clearly defined responsibilities allowing them to perform their duties without costly litigation.

The court found that policy militates against judicial expansion of the trustee's duties. Recognizing a duty running to subsequent purchasers of the property would upset the balancing of interests among beneficiaries, trustors, and trustees. If the duty were provided to the initial subsequent purchaser, then it would also need to be provided to every other subsequent purchaser and would throw into doubt the ownership of every property that has been the subject of a foreclosure sale.

The foreclosure sale was not intended to affect anyone other than the parties to the deed of trust and the successful bidder at the sale. Similarly, the substitution of trustee and partial deed of reconveyance were not intended to affect any parties other than Union Bank and the Peppertree.

Alternatively, the court found no liability based upon negligence because the title problem was discoverable by Heritage. Because there had been a finding of mutual mistake between First American and Peppertree and the court had granted reformation of the deed of trust to cure that mistake, First American could not have created a foreseeable title flaw. But if there was a flaw, then it could also be detected by Heritage Oaks because the substitution of trustee and partial deed of reconveyance was a recorded document.

Equitable indemnity is apportionment based on fault and requires a determination of fault on the part of the alleged indemnitor. Because First American had already been cleared of fault and there can be no indemnity without liability, Heritage Oaks could not state a cause of action for equitable indemnity against First American.

Reporter's Comment: The underlying facts in this case are unique; this makes it hard to predict very much about the future applicability of this holding. A foreclosure sale is not likely to be conducted too often by the wrong trustee as the result of a mutual mistake between the trustor and beneficiary as to the meaning of an earlier substitution of trustee (and which error is then ultimately forgiven by a judicially ordered reformation), which makes this case unlikely to ever work as direct precedent for anything else.

But what can happen in run-of-the-mill cases for a wrong trustee to sell (perhaps because of a forgotten substitution), or for the right trustee to sell the wrong property, or to make some other kind of mistake, which will then force a court to decide the trustee's liability and to whom?

The court's holding that trustee duties are limited to those "imposed by statute or specified in the deed of trust," taken literally, makes it seem that most of the time the trustee should not be liable because no duty was breached. A typical deed of trust only requires the trustee to record notice of default, give notice of sale, sell the property, deliver a deed to the purchaser, and disperse the sales proceeds. Our foreclosure statutes, mainly in the CC §2924s, merely fill in the details of these responsibilities. Since, typically, nothing is said in either those statutes or the deed of trust about the trustee being the one legally authorized to sell (or about, e.g., selling the right property), a trustee who gets it wrong seems unlikely to be held negligent under that standard.

There are also recitals in the trustee deed about the property that was sold (and these recitals are themselves authorized by the deed of trust and also by statute), but those recitals are also mainly limited to the details of the foreclosure sale steps that were taken by the trustee and do not cover the problem of an unauthorized trustee, such as occurred in this case. If those recitals establish the full scope of duty, then a similarly errant trustee – even if not protected by a subsequent reformation order – may be similarly unworried about those recitals. They are by no means the equivalent of the implied warranty of title or right to convey that a grant deed includes. See CC §1113.

The court's alternative holding of the nonforeseeability of remote purchasers is further protective of the careless trustee, although in a different direction. If a later purchaser is to be expected to discover the trustee's lack of authority to sell from her own search of the records (as readily as the trustee could have done), that should not only protect the unauthorized trustee, but may also insulate it from other kinds of mistakes that would constitute negligence even under these more restrictive tests.

Reporter's Comment 2: On this foreseeability issue (which looks like a sort of lack of privity defense), the Heritage Oaks decision gives to immediate foreclosure purchasers more protection than is given to remote purchasers, on the likelihood that the latter have probably obtained title insurance. (That is certainly true, since any rational consensual purchaser would condition its offer on title being marketable as well as insurable by a title company, whereas the immediate direct purchaser at a foreclosure sale generally must make a bid that is unconditional, and will most likely not have incurred the cost of a title search before making its bid.) The greater protection given to a first purchaser may often be offset by the fact that he is usually the foreclosing beneficiary, directly involved in the sale, and perhaps part of the cause of the problems that followed. Nevertheless, if the first purchaser is truly innocent, and the trustee truly negligent (and if there is no reformation defense to save it), then there may be trustee liability.

Reporter's Comment 3: The Peppertree property involved in this case is perhaps the most litigated piece of California land in recent foreclosure history. There is page after page of Westlaw citations to litigation concerning it, including the famed Supreme Court decision involving multiple security. See *Dreyfuss v Union Bank* (2000) 24 C4th 400, 101 CR2d 29. If the Heritage people incurred only some $500,000 in attorney fees, they must have gotten a discount from their lawyers.

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

MORTGAGES; FORECLOSURE; STRICT FORECLOSURE; TIMESHARES: Timeshare properties are eligible for the protections available under the Fair Foreclosure Act and, if they are the residence of the mortgagee, whether primary or not, the court rule that permits the mortgagee, under certain circumstances, to obtain title to the property without a sheriff's sale applies to such timeshare properties. ***Atlantic Palace Development, LLC v. Robledo, 396 N.J. Super. 171, 933 A.2d 48 (Ch. Div. 2007).***

A mortgagee that was in the process of foreclosing on a property sought an exception available under court rules that would have allowed it to gain title to the property in place of having it auctioned at a sheriff's sale. According to the rule, if a mortgagor does not respond to a foreclosure complaint, then title to the property can be vested in the mortgagee. The rule only applies to residential mortgages. When the mortgagee applied for the entry of an order to fix the amount, time, and place to redeem the property, the court administrative office handling such matters refused to process the request because the property in question was a timeshare and, in its mind, not a residential property.
The Court noted that the rule in question states that the mortgaged property must be residential in nature for the exception to take place, but that the rule did not specify whether the mortgaged property had to be the primary residence of a mortgagor for the rule to apply. The Court also noted that a statute mirroring the court rule was passed by the legislature (the Fair Foreclosure Act) and, in it, the term "primary," which was in reference to a residence, was removed. The Court further noted that timeshare statutes allow such properties to be encumbered by mortgages and to be the subject of foreclosure actions. It held that, given the remedial aspects of foreclosure statutes, the legislature did not intend to exclude timeshares from the available protections under the Fair Foreclosure Act.

Having found that timeshare properties could have been subject to the exception available for foreclosures on residential properties, the Court then examined whether the timeshare property at issue was a residential property, noting that the public offering statement said that the timeshare properties were intended for personal use and not to be used as investment properties. The Court found that these particular mortgagors intended to personally occupy the timeshare and, as a result, the mortgaged property was residential. It also found that other conditions necessary to apply the rule applied, such as that the mortgagors had abandoned the property and there was no remaining equity in the property.

MORTGAGES; GUARANTEES; LETTERS OF CREDIT: Party obtaining letter of credit to provide partial guarantee for real estate loan may not assert equitable contribution or subrogation claims against other loan guarantors. ***Morgan Creek Residential v Kemp 153 CA4th 675, 63 CR3d 232 (2007),*** discussed under the heading: "Letters of Credit; Co-guarantors; Contribution."

MORTGAGES; INSURANCE; MORTGAGEE'S INTEREST: A holder of a deed of trust that credit bids the full amount of the debt is not also entitled to insurance proceeds resulting from damage to the secured property, where the property damage occurred **prior** to foreclosure. ***Countrywide Home Loans v. Allstate Insurance Company, 2007 WL 4481007 (Mo.App. W.D.), ___ S.W.3d ___ (Mo. Ct. App. 2007).***

Washington owned a home secured by a deed of trust held by Countrywide. On January 30, 2002, the property was damaged by a fire. On February 19, 2002, Washington notified Countrywide of the loss. Subsequent to the fire, Washington made a claim to Allstate Insurance Company for insurance proceeds, as the property was insured up to $105,280. Despite owing Countrywide $53,793.72, Washington faxed a copy of a forged cashier's check representing to Allstate that he had paid down the mortgage to $8,730.33.

In fact, Washington was in default on the Countrywide note, and Countrywide foreclosed on the property on April 3, 2002 and purchased it at the foreclosure sale for the total indebtedness of $53,793.72.

Thereafter, in response to the earlier communication from Washington, Allstate issued two checks on April 10, 2002: one for $8,730.33 made payable to Countrywide, and one for $96,549.67 made payable to Washington. Washington then forged Allstate's signature on the first check and cashed both checks.

When Countrywide discovered that the foregoing events had occurred, it brought suit against Allstate and Washington for breach of contract, fraud, and tortuous interference of contract. The trial court ruled in favor of Countrywide, causing Allstate and Washington to appeal. On appeal, the court addressed the following issues: (1) whether Countrywide's interest as a mortgagee under the insurance policy was extinguished after it purchased the property for the full amount of indebtedness at the foreclosure sale; and (2) if so, whether the presence of a union mortgage clause in an insurance policy trumps the legal effect of a subsequent foreclosure where the debt was satisfied by the mortgagee's bid.

With respect to the first issue, despite Allstate's and Washington's attempt to distinguish prior cases, the court quickly dismissed their arguments, holding that whether the property damage occurs before or after the property is purchased at a foreclosure sale, the purchase of the property for the full amount of indebtedness extinguishes the mortgagee's interest. However, the court devoted more attention to the second issue, to which there was arguably conflicting precedent.

The union mortgage clause in this case stated that Allstate would "protect the mortgagee's interest in a covered building structure in the event of an increase in hazard, intentional or criminal acts of, or directed by, an insured person, failure by any insured person to take all reasonable steps to save and preserve property after a loss, a change in ownership, or foreclosure if the mortgagee has no knowledge of these conditions." The court cited several Missouri cases which "give credence to the right to insurance proceeds by the mortgagee because of these clauses." Allstate argued that based on these cases, the language of this clause controlled, despite the general principle that a mortgagee's interest is extinguished after it purchases the property for the amount of the debt owed at a foreclosure sale. In addressing this argument, the court cited *Northwestern National Insurance Co. v. Mildenberger*, 359 S.W.2d 380 (Mo. App. Ct. 1962), noting that the "controlling factor is the relative timing of the loss and the foreclosure." When the property loss occurs *before* the foreclosure, the presence of a union clause will not serve to provide the mortgagee insurance benefits beyond the amount of the debt secured.

In addition to clarifying Missouri law with respect to this issue, the court also discussed two public policy reasons not to allow this scenario to occur. First, if these union mortgage clauses are given legal effect over the general rule that a party's interest as mortgagee terminates upon its purchase of the property at a foreclosure sale, the mortgagee/purchaser would receive a windfall in the amount of the difference between the total insurance proceeds and the indebtedness owed. In addition, the court stated that the purpose of union mortgage clauses is limited to keeping the mortgagor from defeating the rights of the mortgagee vis-à-vis the insurance company, and "[i]n no event [is the mortgagee] to collect more than the balance due on the note regardless of source."

Comment 1: This is a lesson that is reasonably well established, but still, it seems, courts and lawyers have a hard time with it. If you participate in a public auction and bid a certain amount for property, it is likely that the value you bid will be viewed as the appropriate value for measuring your rights in the future. If you're a mortgagee, and bid in full value, you've been paid.
The last time DIRT reported a case making this point was four years ago: *Lenart v. Ocwen* Financial Corp., 869 So. 2d 588 (Fla. App. 2004), the DIRT DD for 11/9/04.

Comment 2: In fact, the editor has an article on these issues: P. Randolph, The Mortgagee's Interest in Casualty Loss Proceeds, Evolving Rules and Risks, 32 ABA Real Property, Prob. & Tr. Law J. 1 (1997) (which the Court of Appeals in the Editor's own state callously ignored here.) In the article, the Editor discusses the position of the Restatement of Mortgages, which was then just coming out. The Restatement, and in fact all relevant authority, support the outcome here, but there are some interesting disagreements on other, related issues.

What if the mortgagee forecloses after the property is damaged, but the mortgagee knows nothing of the damage [not the case in the instant DD]? This could occur either because the mortgagor has disguised the damage or because the damage occurred so soon prior to the sale that the mortgagee didn't find out about it. The mortgagee's bid at foreclosure will reflect its perception of the value of the property in its undamaged condition. Thus, it might bid in full value, or the deficiency in any event will be smaller than it otherwise might have been. Should the deficiency be the sole measure of the mortgagee's protection here? The Restatement says yes – on the theory that careful mortgagees should check the property just before foreclosure, and in any event the injustice of the "hard cases" that will arise is offset by the benefits of a clear rule. The editor disagreed in his article, arguing that the mortgagee should be permitted to demonstrate that for excusable reasons the mortgagee was unaware of the damage. (Probably if the mortgagor actively disguised the damage, the court might view that as a basis for giving the mortgagee a greater share of the proceeds, but the Editor knows of no cases on the point.)

Comment 3: In the present case, the mortgagor misrepresented the status of the mortgage to the insurer and forged the mortgagee's name on a check. He was certainly a bad actor, and perhaps this is the reason that the trial court spanked him by finding for the mortgagee. But the mortgagee was well aware that the property had been burned at the time it bid at the sale. It should live with its bid!!

The only new argument here was the argument based upon the language in the standard mortgagee clause in the insurance policy. It says that the insurer must protect mortgagee's interest. But the mortgagee's interest only is to be paid the amount it is owed. When it bought the property for the full amount owed, the mortgagee satisfied the debt, and had no further interest to protect.

RECORDING ACTS; REGISTRATION; "ACTUAL KNOWLEDGE:" The presence of electricity poles and use of electricity by a property owner do not prove the property owner had actual knowledge of the location of an easement for purposes of amending the certificate of title to registered land***. Commonwealth Elec. Co. v. MacCardell, 876 N.E.2d 405 (Mass. 2007).***

Commonwealth Electric Company ("Commonwealth") sought to install a transformer on an electric pole located on the property of Leslie H. MacCardell ("MacCardell"). The poles were placed on the property years before pursuant to an easement deed granted by a prior owner to Commonwealth's predecessor. Although that easement deed did not identify the precise location of the right of way, the electric pole and accompanying wires were installed on the property.

Later, after a subsequent owner filed a successful action to register title to the property in the land registry, the issued certificate of title to the property mistakenly omitted a reference to the easement. (The easement was shown on the certificate of an adjacent parcel.) When MacCardell purchased the property, she received this certificate of title, which had not been corrected.

Commonwealth petitioned the Land Court to amend the certificate of title based on the mistake and the physical presence of the poles, but the court found for MacCardell and the appeals court affirmed. "[S]ubsequent purchasers of registered land for value and in good faith take free from all encumbrances except those noted on the certificate [of title]." Easements also must be shown on the certificate to bind such good faith purchasers.

The court noted two exceptions to this rule: First, where the certificate describes facts that would lead a reasonable person to inquire further; and second, where the buyer has "actual knowledge" of the easement.

Here, the Supreme Judicial Court considered only the second exception, explaining that actual knowledge requires "some intelligible oral or written information that indicates the existence of an encumbrance or prior unregistered interest." The Supreme Judicial Court held that the mere presence of the poles and MacCardell's use of electricity did not sufficiently prove actual knowledge of the easement on her part and that the registered land statute did not allow the court to imply an easement by prescription.

Comment 1: Of course, in most recording theory states, the existence of conditions on the ground puts one on inquiry notice of what interests those conditions might signify, and probably first on the list are lines and poles. Note that it is likely that MacCardell probably had actual knowledge of the presence of the lines and poles when she acquired the property, but this also doesn't seem to matter to the court.

This case underscores the significance of registered title regimes in providing clear title, and also underscores some of the problems with the system.

Comment 2: One wonders whether there is an action for negligence either against the registrar or some other party for the erroneous deed. One assumes that in the original action to register title, Commonwealth would have had to have been a named party, since it apparently had a recorded easement at that time. Was Commonwealth negligent in not following up to be sure that the final registration incorporated its interest?

Comment 3: The court at first appears to assume that its rule would apply even if the landowner had actual knowledge of the presence of poles and lines on the land at the time of purchase. But later it states that one reason for protecting the landowner in this case is the fact that the average lay person does not know the exact boundaries of his or her land. This may suggest that where, in fact, a landowner had actual knowledge, such as through a survey, of an encroachment or other competing structure, a court could distinguish the present case. But don't hold your breath.

SERVITUDES; MODIFICATION; ASSESSMENTS: An Association may not raise the annual maintenance charge set forth as a servitude in the master deed if the master deed limits such increases, but, if overall development and use scheme cannot be realized by fees set forth in master deed, and public policy demands, a court may modify the servitude to provide for increases. ***Citizens Voices Association v. Collings Lakes Civic Association, 396 N.J. Super. 432, 934 A.2d 669 (App. Div. 2007).***

SERVITUDES; RESTRICTIVE COVENANTS; USE RESTRICTIONS; "NO COMMERCIAL USE;" DAY CARE. A homeowner's operation of a licensed day care out of her home, caring for up to twelve children daily, constituted a commercial use in violation of a housing development's restrictive covenants prohibiting commercial enterprise, but a facility with fewer children might not. Public policy favoring home day care was not violated by enforcement of the housing development's restrictive covenants. ***Lewis-Levett v. Day, 875 N.E.2d 293 (Ind.App. 2007).***

In October, 2005, Jeannie Lewis-Levett ("Lewis-Levett") purchased a residence in the Golfview Estates housing development. The original developers and, later, Richard and Martha Day (the "Days"), as successor owners and developers, recorded instruments evidencing restrictive covenants applicable to the lots in Golfview, including Lewis-Levett's. These restrictive covenants prohibited any lot or building from being used for business or commercial purposes.

In November, 2005, Lewis-Levett began operating a licensed child day care in her home through which she cared for up to twelve children on a daily basis. The Days filed a complaint requesting a temporary and permanent injunction against Lewis-Levett's operation of a child care home in her residence, and subsequently filed a motion for summary judgment. The trial court granted summary judgment in favor of the Days, enjoining Lewis-Levett from operating a licensed day care home and awarding attorneys fees.

Lewis-Levett appealed and the Days cross appealed. On appeal, Lewis-Levett argued that the operation of a licensed day care is a residential use and, therefore, such use does not violate the restrictive covenants. Alternatively, she argued that if the operation of a licensed day care was deemed to be a business use of her home, the enforcement of the restrictive covenants would violate Indiana public policy in favor of home day care.

In support of her first argument, Lewis-Levett cited to *Stewart v. Jackson*, 635 N.E.2d 186, 193 (Ind.Ct.App. 1994), which held that the operation of an unlicensed home day care constituted a residential use, and therefore, did not violate restrictive covenants that prohibited commercial use of lots in a residential neighborhood. The Court, however, distinguished *Stewart* after a consideration of the number of children in the day care, the income generated by the day care, and the increase in traffic produced by the day care. Lewis-Levett cared for three times more children than the defendant in *Stewart*, used sixty percent of her home for business purposes, and had up to twelve vehicles entering and exiting the subdivision twice a day. The Court concluded that Lewis- Levett's day care operation was more than just a slight departure from residential use.

The Court also concluded that although Indiana has a strong public policy in favor of home day care, that policy did not justify the obtrusive impact of Lewis-Levett's licensed home day care on her neighbors. Indiana's legislature created a board to coordinate child care regulation and enacted licensing statutes governing home day care. The legislature's choice to regulate only licensed, and not unlicensed, home day care, indicates that it intended unlicensed home day care to be considered a residential use, while larger home day care operations that require licenses, such as Lewis-Levett's, are considered to be commercial enterprises.

The extensive regulations of licensed home day care operations indicates that the public policy in favor of home day is not without limits. The public policy favoring home day care does not supersede otherwise legitimate restrictive covenants prohibiting the use of lots in a housing development for commercial purposes. The Court therefore found that Lewis-Levett's commercial use of her residence was not justified by Indiana's public policy support of licensed home day care operations.

The Court then denied the Days' cross appeal contending that the trial court erred to the extent that it did not enjoin Lewis-Levett's operation of any day care in her residence. Because the trial court did not properly have before it the case of an unlicensed home day care, the Day's cross appeal was not properly before the Court.

Comment 1: It is interesting that Indiana precedent appears to view "business" and "residential" as opposite concepts, at least in construing restrictive covenants. If a use is "residential," then it appears that it is not "business" or "commercial." Of course, this saves all those Ebay entrepreneurs operating out of their garages, presumably, as well as accountants, lawyers, authors (technical and otherwise) and a host of other "home based business persons." And it may in fact be consistent with the overall purposes of the restriction – which really is to control outside manifestations of business activity, rather than to prohibit residents from conducting activities within their homes that may earn some income. Also see: *Gabriel v. Cazier*, 938 P.2d 1209 (Idaho 1997) (the DIRT DD for 12/3/97) (A covenant prohibiting "business or trade" activity in a subdivision does not prohibit swimming lessons conducted by a homeowner's children for profit during the summer months.)

Comment 2: One of the more interesting aspects of the case is the proposition, taken seriously by the court, that the public policy in favor of neighborhood day care ought justify striking down private restrictions prohibiting neighborhood day care. There is some precedent, of course, for this, since the new Restatement takes the position that public policy ought to motivate courts to set aside covenants that restrict activities that the judges think are valuable to the society. Frequent readers of these reports know that the editor strongly disagrees with this sort of thinking. *Also see: Terrien v. Zwit*, 467 Mich. 56, 648 N.W.2d 602 (Mich. 2002) (The DIRT DD for 10/10/02) (Michigan rejects notion that court established public policy should be used to invalidate private land use covenants; consequently restriction prohibiting businesses in residential subdivision prevents use of home as a "family day care center.")

The court also cites Indiana precedent that restrictions on use of land are still disfavored in Indiana and will only be permitted when they don't violate public policy. This is something of an old fashioned view, and one isn't certain how seriously courts really take this precedent. But it is interesting that Indiana continues to cite it, even though in general Indiana seems to be a "freedom of contract" court.

SERVITUDES; RESTRICTIVE COVENANTS; DURATION: A duration of "forever" in a restrictive covenant is unreasonable as to time, making the covenant invalid. ***Citibrook II, L.L.C. v. Morgan's Foods of Missouri, Inc., ___ S.W.3d ___ (Mo. Ct. App. 2007).***

Citibrook owned property in St. Louis and held franchise rights to operate a Kentucky Fried Chicken (KFC) restaurant on the property. In 1982, Citibrook transferred ownership of the property to Kirkwoods by general warranty deed, which provided in pertinent part that the grantor "for itself and its successors in interest forever restricts the above described transfer in the following manner: "The use of the described property is hereby restricted to the erection and operation of a Kentucky Fried Chicken store and may be used for no other purpose."

Kirkwoods acquired franchise rights to operate a KFC and operated a KFC on the property until transferring it to Morgan's Foods in 1999. Until 2004, Morgan's Foods also operated a KFC on the property. In April 2005, however, Morgan's Foods executed a lease for the property with a J.J.'s Fish and Chicken outlet. Subsequently, a J.J.'s Fish and Chicken restaurant opened on the property.

Citibrook filed for injunctive relief against Morgan's Foods in October 2005, alleging that the restrictive covenant in the 1982 warranty deed prohibited any business from being operated on the property except for a KFC. It also filed a motion for summary judgment, asserting that by operating a J.J.'s Fish and Chicken on the property, Morgan's Foods violated the restrictive covenant. Morgan's Foods countered with its own motion for summary judgment, arguing that the restrictive covenant contained in the deed was void and unenforceable because it violated public policy and constituted an unreasonable restraint on trade and alienation of the property.

The trial court granted Morgan's Foods' motion, finding that the restrictive covenant was "unenforceable, invalid, void, and of no effect . . . because it is unreasonable on its face, unreasonable in duration, repugnant to trade and commerce, contrary to business interests and endeavors in the area [of the property], is not favored by law, and has the effect of creating a monopoly."

On Citibrook's appeal, the primary issue the Missouri Court of Appeals addressed in determining the covenant's validity was whether the duration of "forever" was unreasonable as to time. The court began by noting that Citibrook's alleged purpose of the restrictive covenant ("to provide a well- recognized, top of the line national franchise" on the property) was not expressed in the language of the covenant itself, and thus couldn't justify it. Instead, the court found the language of the covenant (the use is "restricted to the erection and operation of a [KFC] store and may be used for no other purpose") unambiguous. Therefore, it refused to incorporate any other purpose.

The court stated that Missouri law provides that a restrictive covenant will not be upheld unless it is clear that the restriction against the use of land is "reasonable as to time," citing both *Hall v. American Oil Co.*, 504 S.W.2d 313, 317 (Mo. Ct. App. 1973), and *Dean v. Monteil*, 239 S.W. 2d 337, 340 (Mo. 1951). Citibrook responded that *Hall*, in fact, upheld a competition restriction and stood for the proposition that such restrictions should be upheld.

In *Hall*, the plaintiffs wished to enter into a lease with Shell Oil Company, which intended to build an auto filling station on the plaintiffs' land. American Oil Company, however, owned land adjacent to the plaintiffs' land, and the plaintiffs' deed contained a restrictive covenant that burdened their land, providing that use was "restricted against the erection and operation of an Auto Gas Filling Station and the dispensing and sale of Petroleum Products . . . for as long as an Auto Filling Station shall be operated on [American Oil Company's] property." The court in *Hall* refused to strike down the time limitation in the restrictive covenant, reasoning that it was not necessarily oppressive, it could be compatible with the purpose of the covenant, and in many instances was less onerous than a restriction for a large number of years where the purpose of the restriction ceases to exist.

In the present case, the court of appeals distinguished *Hall* for two reasons. First, the indefinite time limitation in *Hall* ("as long as an Auto Filling Station shall be operated on [American Oil Company's] property") and the restrictive covenant's purpose of preventing plaintiffs from operating an auto filling station on their property were compatible because they involved the same subject matter and were directly related to one another. Here, the indefinite time limitation "forever" and the purpose of the restrictive covenant (as noted above) were not directly related. Second, while the time limitation in *Hall* was indefinite, there was still a potential end to the covenant if American Oil Company ceased to operate an auto filling station on its property. Because "there is no potential end to 'forever,' it is impossible for the indefinite time limitation in this case to be less onerous than a restriction for a large number of years." For those reasons, the court ultimately held that the duration "forever" was unreasonable as to time, making the restrictive covenant invalid.

Comment 1: The editor was not aware that there was a public policy declaring that perpetual easements are unenforceable *per se* as this case suggests. Indeed, there is significant authority, backed up by the Restatement of Servitudes, that where no duration is stated in a restriction, the duration is *presumed* to be perpetual. Restatement of Property (Third) – servitudes Sec. 4.3 (2000). See, generally, Gerald Korngold, Private Land Use Arrangements: Easements, Real Covenants and Equitable Servitudes (Juris 2nd Ed. 2004). Sec. 11.01.

The editor remains dubious that the a perpetual servitude is invalid *per se*, even in a jurisdiction, like Missouri, that states that it interprets restrictions strictly to preserve the free enjoyment of land.

Comment 2: The cases cited by the *Citibrook* court, and those relied upon by those cases, all involve anti-competition covenants. In what might be the classic case, *Shephard v. Spurgeon,* 365 Mo. 989, 291 S.W. 2d 162 (Mo. 1956), landowners transferred a 300 acre parcel along the Iowa/Missouri border highway and reserved for themselves a one acre parcel along the highway. Covenants provided that for 100 years there could be no commercial use of the 300 acre parcel, but that the one acre parcel was free from any commercial constraints. The obvious purpose, stated the court, was to create a 100 year monopoly for the sellers and their successors. The court deemed this to be repugnant to public policy, and the 100 year term was relevant to the evaluation of the covenant. *Dean v. Monteil*, 239 S.W. 2d 337, 340 (Mo. 1951), quoted by the *Citibrook* court, had similar facts. Indeed the court did say that covenants had to be reasonable as to time, but this was just part of a larger statement addressing specifically anti-competitive covenants, and why they should be treated differently. Duration was only part of the analysis, and the analysis clearly did not apply to covenants that were not anti-competitive in nature:

"The restrictions in this case cannot be sustained on the theory that a residential district was created. That was not the main purpose of the agreement. To uphold the restrictions now would serve the sole purpose of restricting competition in business. Such restrictions have been upheld within certain limitations. In *Mallinckrodt Chemical Works v. Nemnich,* 83 Mo.App. 6, as page 14, the court said, 'The general doctrine is that agreements in restriction of trade will be upheld when the restriction does not go beyond some particular locality, is founded on a sufficient consideration, and is limited as to time, place and person.' Then at page 16 of 83 Mo.App. we find the following: 'This class of contracts is always regarded with suspicion by the courts, as their effect usually is to create a monopoly, and before any one of them will be upheld, it should clearly appear that no monopoly is created by it; that its enforcement will not prejudice the public; that it is reasonable as to time, space and person, not oppressive or injurious, and that the contract is founded on a good consideration, and that its enforcement will be useful and beneficial to the promisee'."

It is from that analysis that the instant court got the general statement that covenants that are not reasonable as to time offend public policy, leading to the conclusion that perpetual covenants will almost always offend public policy. Neither of these conclusions is supported by the authority cited by the court or, the editor's knowledge, by any other authority. The court retains the tool of the "changed circumstances" doctrine to delimit the impact of a covenant when too much time has passed. But there is no reason to strike down the covenant at the outset on the basis of its perpetual nature.

Comment 3: Turning to the covenant in this case, it appears to be questionable whether the purpose of the covenant was to create a monopoly. Indeed, the benefitted parties argued that the purpose was to maintain a high end (if that's possible) fast food outlet at the location, and KFC was chosen because that's what was there. There is no indication that the benefitted parties had a specific profit interest in KFC.

Comment 4: Gerry Korngold, author of the treatise cited above, contacted by the author, opined that the outcome is sound, but not for the reasons stated by the courts:

"[T]he restriction is functionally similar to a direct restraint on alienation, as it in effect limits the ownership of the property to a very limited group of people (*i.e.*, KFC or a franchisee). Who else but such a party could own the property? This creates a significant restraint on alienation. Private arrangements between parties are generally a good thing, deserving enforcement except in rare circumstances. A major clog on the marketplace, such as is created by the perpetual covenant here, is a circumstance where there should be no enforcement."

Comment 5: Susan French, Reporter of the Servitudes Restatement, also contacted by the author, had this to say:

"I think this covenant could properly be held invalid either as an unreasonable restraint on alienation or an unreasonable restraint on competition. Duration is relevant in both those determinations. For many other kinds of servitudes, however, unlimited or indeterminate duration is entirely appropriate, as the Restatement recognizes. Context matters."

Comment 6: The editor agrees with both of the above comments, in general, although he doesn't see why this particular covenant could be regarded as anti-competitive.

But neither of these comments really supports the case as it is written. The court's opinion cannot be read so narrowly as to apply only to anticompetitive covenants or covenants that very narrowly constrict transfer rights. Rather it appears to say that a perpetual covenant is unreasonable, at least in most cases. This does not support precedent, and is likely to cause havoc as precedent in the future. In short, the court completely messes up precedent and misapplies the rules to reach an anomalous result. This is a poorly analyzed decision. Fortunately, this being a St. Louis court, the judge's clerk likely was not one of UMKC's graduates.

STATE AND LOCAL TAXES; PROPERTY TAX; ASSESSMENTS; VALUATION CHALLENGES: A property owner owning improved property may not challenge only the land or improvement components of its valuation separately; rather, the owner must allege that the appraised value of the property as a whole is not equal or uniform. ***Covert v. Williamson Central Appraisal District, ___ S.W.3d ___ (Tex. Ct. App. 2007).***

Coverts owned five tracts of land, three of which were improved with car dealerships. The Coverts filed suit in district court against Williamson Central Appraisal District (WCAD), challenging four tax year valuations of the five tracts. The Coverts sought to modify their challenge to appeal the valuation of "the land portion only" of each of the tracts, arguing that the land underlying their car dealerships had been appraised unequally when compared to other vacant, unimproved parcels near their property. In response, the WCAD argued that the applicable tax code did not provide a remedy for a taxpayer contesting only the land portion of an appraisal. The trial court agreed with WCAD, and ordered the Coverts to replead their cause of action to the effect that the entire property was appraised unequally. The Coverts refused to do so and the trial court dismissed the case.

On appeal, the Texas Court of Appeals addressed, as a matter of first impression, whether a taxpayer may challenge a single component of the assessor's appraisal of improved land under the applicable statute. The court began by highlighting the text of the statute, which provided that the court "shall grant relief on the ground that a property is appraised unequally if the appraised value of the property exceeds the median appraised value of a reasonable number of comparable properties appropriately adjusted." The Coverts argued that nothing in the statute required them to challenge every item comprising "property," and that the intent of the legislature was to narrow the median test "to whichever matter or thing was selected for challenge by the property owner." In support of this argument, the Coverts pointed to: (1) the fact that the indefinite article "a" preceded the word "property" in the provision; and (2) a separate provision in the statute which required the appraisal district to separately list values for land and improvements.

The court held that "the choice of article antecedent to the word 'property'" was not clear evidence of the legislature's intent; rather, "whatever property is *appraised* must be valued equally in relation to other comparable properties." With improved property, a single value is given to the entire property, and an owner may only prevail in a challenge to that value if the owner shows that the appraised value of the improved property is not equal or uniform. Further, the court noted that land improved with particular features (such as a car dealership) has different characteristics affecting its market value than undeveloped land. Ultimately, while the separate value of land or improvements can be brought as evidence in a valuation challenge, the court refused to allow the Coverts to challenge the component values of their property in isolation from a consideration of the total assessed value. Instead, it held that a property owner must allege that the overall appraised value is unequal.

Comment: The problem with the outcome from the standpoint of the appellants is that the appraiser has huge flexibility in setting values, as improvements such as car dealerships are not readily comparable to one another. But the remedy may be legislative.

TIMESHARES; FORECLOSURE: Timeshare properties are eligible for the protections available under the Fair Foreclosure Act and, if they are the residence of the mortgagee, whether primary or not, the court rule that permits the mortgagee, under certain circumstances, to obtain title to the property without a sheriff's sale applies to such timeshare properties. ***Atlantic Palace Development, LLC v. Robledo, 396 N.J. Super. 171, 933 A.2d 48 (Ch. Div. 2007)***, discussed under the heading: "Mortgages; Foreclosure; Strict Foreclosure; Timeshares."

TITLE; REGISTERED TITLE; "ACTUAL KNOWLEDGE:" For purposes of construing whether a purchaser of registered title was in "good faith" the presence of electricity poles and use of electricity by a property owner do not prove the property owner had actual knowledge of the location of an easement for purposes of amending the certificate of title to registered land**. *Commonwealth Elec. Co. v. MacCardell, 876 N.E.2d 405 (Mass. 2007).*** , discussed under the heading: "Recording Acts; Registration; "Actual Knowledge."

TITLE INSURANCE; EXCEPTIONS TO COVERAGELANGUAGE CONSTRUCTION: In a title insurance policy containing an exception for coverage with respect to "Restrictive Covenants affecting the property described in Schedule A," the phrase "described in Schedule A" modifies only the word "property," resulting in an exception for all such covenants of record as of the date of sale. ***Cobb v. Stewart Title Guaranty Co., ___ S.W.3d ___ (Tenn. Ct. App. 2007).***

Clinton Cobb purchased and obtained title insurance for two tracts of land, intending to market the two tracts as separate properties and improve them with upscale residences. Subsequent to his purchase, Cobb discovered that the restrictive covenants (in effect at the time of purchase) forbid such use of the land. As a result, Cobb submitted a claim against Stewart Title Guaranty Co. due to problems caused by the restrictions, and brought suit after it refused to pay. The title insurance policy was comprised of the standard Schedule, which contained a description of the property, and Schedule B, which provided that the policy "does not insure against loss or damage (and the Company will not pay costs, attorney's fees or expenses) which arise by reason of: . . . 8. Restrictive Covenants affecting the property described in Schedule A." The trial court granted Stewart Title's motion to dismiss, holding that the policy specifically and unambiguously excluded restrictive covenants from its coverage.

On appeal, Cobb argued that the phrase in Exception 8 was ambiguous, and asked the court to read the phrase "described in Schedule A" as modifying the entire phrase preceding it, rather than merely modifying the word "property." In that regard, Cobb argued that the exception would exclude only those restrictive covenants specifically described in Schedule A, with the result that all other covenants would be covered by the policy. The court dismissed this argument, noting that the interpretation "is contrary to the plain meaning of the language of Exception 8 and also contrary to a reasonable and logical construction of the contract as a whole," and stating that it "is not the covenants that are described in Schedule A, but the property." Further, a contrary reading of the exception "would render it effectively meaningless and superfluous."

TITLE INSURANCE; INSURER'S DUTY TO NON-INSUREDS: Title insurer may have duties to non-insureds who forseeably rely – at least where insurer leads such parties to believe that they can rely upon search and policy provided earlier. ***Barrington Reinsurance Ltd., LLC v. Fidelity Nat'l Title Inc. Co., 172 P.3d 168 (N.M. App. 2007).***

A nonparty to the action, Mr. Freeze ("Freeze"), acquired two lots, 8 and 9, from another nonparty, Mr. Turner. When Freeze acquired the lots, he obtained an Owner's Policy of title insurance from Fidelity National Title Insurance Company ("Fidelity"). The Policy that was issued did not indicate or except any restrictive covenants on the two lots. But in fact, as will develop, there was an important restriction that the insurer overlooked.

Two months later, Freeze deeded both lots to the plaintiff, Barrington Reinsurance Ltd., LLC ("Barrington"). As the appellate court noted, "Freeze and Barrington retained Fidelity to act as closing agent, to provide advice, and prepare documents in regard to the transfer of Lots 8 and 9."

A few months after the closing (without title insurance), Barrington entered into a contract to sell Lot 8 for $480,000, and retained Fidelity to conduct a title search in connection with the issuance of an Owner's Policy of title insurance to the purchaser. During this search, Fidelity discovered a recorded agreement that somehow had been overlooked in its previous title searches on the property, which agreement provided that Lot 8 and Lot 9 could not be sold separately and that only one house could be built on the two lots (unfortunately, a house already existed on Lot 9), and therefore Barrington could not sell Lot 8 to the prospective purchaser.

Fidelity acknowledged its mistake, but "failed to solve the problem." Barrington eventually filed an action against Fidelity, asserting the following claims: negligence: negligent misrepresentation; breach of implied or constructive contract; and unfair, deceptive, or unconscionable trade practice. Barrington argued that it relied on the oral representations made by Fidelity in connection with the transfer of Lots 8 and 9 from Freeze to Barrington and, in so doing, did not obtain title insurance. The district court ruled for Fidelity on the negligence claim but concluded that N.M.S.A. § 59A-30-11(A) did not apply to Barrington's remaining claims. N.M.S.A. § 59A-30-11(A) states as follows:

"No title insurance policy may be written unless the title insurer or its title insurance agent has caused to be conducted a reasonable search and examination of the title using an abstract plant meeting the requirements of Section 59A-12-13 NMSA 1978 and has caused to be made a determination of insurability of title in accordance with sound underwriting practices. The duty to search and examine imposed by this section is solely for the purpose of enhancing the financial stability of title insurers for the benefit of insureds under title insurance policies. The New Mexico Title Insurance Law is not intended and should not be construed to create any duty to search and examine that runs to the benefit of, or to create any right or cause of action in favor of, any person other than a title insurer."

Fidelity then appealed to the New Mexico Court of Appeals, to consider the application of N.M.S.A. § 59A-30-11(A) to the remaining claims of Barrington's complaint. (Barrington did not contest the lower court's denial of its claim of negligence under N.M.S.A. § 59A-30-11(A), but argued that it was entitled to relief on all the other counts in its complaint because they did not invoke the application of N.M.S.A. § 59A-30-11(A).)

Fidelity, in its argument to the appellate court, claimed that all of Barrington's claims were based on the title search and therefore all of its claims should be barred under N.M.S.A. § 59A-30-11(A). While the appellate court agreed with the district court's ruling on the negligence claim, and noted that N.M.S.A. § 59A-30-11(A) "is not intended to impose a duty of reasonable care running to the benefit of any person other than a title insurer," it reasoned that the statute did not preclude Barrington's other claims, which were based on events and other duties that were separate from the issuance of the title policy to Freeze. Therefore, the court held as a matter of law that N.M.S.A. § 59A-30-11(A) did not bar recovery based on Barrington's remaining claims.

The appellate court then dealt separately with each of the other grounds argued by Fidelity on appeal (except the negligence claim, as noted above). With respect to Barrington's claim for negligent misrepresentation, the court ruled in favor of Barrington and held that such a "duty is clearly distinguishable from the duty of reasonable care, on which Barrington's claim for negligence was grounded. Thus, we cannot conclude that the failure of Barrington's claim for negligence affects the merits of Barrington's claim for negligent misrepresentation." The court noted that, unlike a claim for negligence in conducting a title search, a claim for negligent misrepresentation rests where a party has a duty to disclose information and to give it with care and the person receiving it has a right to rely and act upon it and does so to his damage. According to the court:

"We read the statute to say that it does not create any additional duty, right, or cause of action running to the benefit of anyone other than an insurer. We do not read Section 59A-30-11(A) to preclude the existence of a duty or prohibit a cause of action that may otherwise exist in common law or by another statute. Based on the plain language of Section 59A-30-11(A), we conclude that the legislature did not intend to preclude liability that is based on a duty arising out of common law or another statute."

Because Fidelity's original summary judgment motion was based solely on N.M.S.A. § 59A-30-11(A), and Fidelity made additional arguments regarding Barrington's claims for breach of implied contract and violation of the UPA for the first time in its appellate reply brief, the court declined to address those arguments. The court summarized its holding on this issue as follows:

"We conclude that Section 59A-30-11(A) does not bar Barrington's claims for negligent misrepresentation, implied breach of contract, and violation of the UPA because these claims are not based on a duty to use reasonable care in a title search. Accordingly, we affirm the trial court's order denying in part summary judgment."

Reporter's Comment 1: This case should serve as a cautionary tale for title insurance companies. It is certainly unusual for a title insurer (against its own – and its customer's – apparent self interest) to suggest to a customer that it not obtain title insurance on a purchase-and-sale transaction, no matter what the "comfort" level of the title insurer may be with respect to the current status of title to the property. The folks in Fidelity's local office undoubtedly had their hearts in the right place (they probably had a close relationship with the customer and wanted to save the customer some money in connection with what appeared to be a "vanilla" transaction). But this is not an area where a title insurer should be making any comments or suggestions at all with respect to the state of the title to the property or the need for title insurance. It was certainly risky for Fidelity to "provide advice and prepare documents in connection with the transfer" when it was not providing (and was in fact discouraging) the issuance of title insurance for the transaction. Id. at 169.

Reporter's Comment 2: It does not appear from a reading of the decision that Barrington had retained an attorney in connection with the transaction. If Barrington had retained an attorney, he or she may have advised Barrington to obtain title insurance regardless of what Fidelity said. Still, Barrington apparently elected not to retain counsel and made its own decision regarding the need for title insurance (albeit based on Fidelity's advice). Barrington had no direct contractual privity with Fidelity with respect to the issuance of title insurance in connection with the sale of the property by Freeze to Barrington, with Fidelity acting only as the closing (and not the title) agent. But the court found that while Fidelity owed no duty to Barrington to exercise reasonable care in conducting a title search under N.M.S.A. § 59A-30-11(A), Barrington's claim of negligent misrepresentation was based on Fidelity's duty to disclose information and not on any duty of reasonable care in the title search. Therefore, the trial and appellate courts rejected Fidelity's attempt to avoid all of Barrington's claims solely based on N.M.S.A. § 59A-30-11(A).

Reporter's Comment 3: Does the failure of an attorney who represents the purchaser of a property to obtain a title commitment and an owner's policy of title insurance constitute legal malpractice? Does — or should — the answer to this question depend on whether the attorney has made full disclosure to the purchaser of the risks of not being insured? Should such a duty extend, under certain circumstances, to third-party non-clients? These questions, which have become more and more common in connection with the duties of attorneys, may now, as the result of the Barrington decision, become problematic for title insurers in certain instances. In the commercial area, title insurance has been virtually mandatory for many years, especially as a result of securitization, lender requirements, and the nationalization of commercial real estate practice and standards. But title insurance as an industry standard has not yet reached total acceptance with respect to residential real estate transactions. Generally, the benefits of title insurance, including no-fault protection for losses covered under the policy, outweigh the risks of not obtaining title insurance. But to suggest that an attorney — or title insurer — violates various contractual or tort doctrines or statutes by advising a fee owner of real estate not to obtain a title insurance policy (or even mentioning that it is available) in connection with a sale of the property, is a step that few courts (or bar associations) are willing to take at the present time. Some commentators have gone so far (perhaps too far) as to state that failing to require a title policy would constitute incompetence (and presumably malpractice) on the part of a lawyer. They argue that with respect to commercial real estate transactions, title insurance has been a de facto requirement for some time, and appear to have no problem extending this duty to residential transactions. See, e.g., Robin Paul Malloy & Mark Klapow, Attorney Malpractice for Failure to Require Fee Owner's Title Insurance in a Residential Real Estate Transaction, 74 ST. JOHN'S L. REV. 407, 426-427 (2000):

In fact, the financial markets, the mortgage providers, and the legal profession would all consider it quite unusual and, indeed, incompetent to do a real estate closing for a lender or commercial developer without providing title insurance to cover the risk of loss from title defects.

These commentators appear to have no problem extending this duty to residential transactions:

"It is our contention that a lawyer commits malpractice in representing a home buyer if that attorney fails to require a fee owner's commitment and policy of title insurance as part of the transaction. We believe that the only exception to this requirement is when the lawyer makes a full disclosure to the client of the risks of not being insured; gives explicit advice against proceeding without insurance; and obtains the client's consent and signature to this effect on a written document. Furthermore, we believe that this obligation may run to a third party non-client in certain situations."

The authors add further that:

"Today, it is widely accepted that title insurance is the only appropriate product to fully protect a homeowner or lender from risk of loss. For this reason the industry standard reflects a duty to obtain fee owner's title insurance for a client as a routine matter in all residential transactions. Ignoring this standard is grounds for a malpractice action. Attorneys can no longer protect themselves in a malpractice action by arguing that the local, antiquated customs, appropriate in bygone decades, control in the modern residential real estate market." Id. at 443-44.

See also Robin Paul Malloy, Using Title Insurance to Avoid Malpractice and Protect Clients in a Changing Marketplace, 11 DIGEST: NAT'L ITALIAN AM. BAR ASS'N L.J. 51, 52 (2003) ("as a result of market changes, a lawyer commits malpractice in failing to obtain fee owner's title insurance for a residential homebuyer. . . . Attorneys that follow local norms that do not include requiring fee owner's title insurance should be held to have committed malpractice"); Kenneth M. Turnipseed, Legal Malpractice and the Real Estate Lawyer, 27 J. LEGAL PROF. 247 (2003) (discussing a few of the most often cited attorney malpractice areas in real estate practice, including incorrect title opinions and failing to inform the client of a flaw in the title to real estate); Thomas W. Hyland, Ellen M. Boratz, Frank J. Fields, Legal Malpractice and the Real Estate Practitioner, 265 PLI/Real 7, 31-32 (1985) (discussing the liability of an attorney for errors in the determination of title); John C. Murray, Attorney Malpractice in Real Estate Transactions: Is Title Insurance the Answer? 42 REAL PROP. PROB. & TR. J. 221, 224 (2007):

Generally, institutional lenders are more sophisticated and perhaps better able to take care of themselves and, therefore, may not need special protection. Thus, the issue of malpractice usually arises in the situation where an attorney fails to recommend title insurance to a purchaser of real estate, or even, in some cases, to a non-client third party.

Reporter's Comment 4: The appellate court in *Barrington* stated that Barrington retained Fidelity "to act as closing agent, to provide advice, and to prepare documents in regard to the transfers of Lot 8 and 9.**"** Such actions, in many states, could constitute the unauthorized practice of law. The past few years have seen a flurry of cases regarding the issue of what constitutes the unauthorized practice of law in connection with real estate transactions. The courts (and applicable regulatory authorities and agencies) have not been uniform in their rulings and pronouncements, which can differ greatly depending on which state is involved. Some states are very jealous of guarding the legal profession — and ostensibly, the public — against what they perceive as the encroachment of other professions and businesses (such as brokers, realtors, title companies, and banks) into the business of providing legal services and advice. Other states are willing to accept "economic reality" and permit nonlawyers to perform what they believe are routine and ministerial "quasi-legal" tasks, such as conducting residential real estate closings and completing (and in some cases, charging for) standardized form deeds, mortgages, and leases, which tasks they believe benefit consumers by reducing the cost of the transaction, increasing competition, and minimizing delays.

Recent cases finding that such actions by a title insurer or its agent constitute the unauthorized practice of law include: *Toledo Bar Ass'n v. Chelsea Title Agency of Dayton, Inc*., 100 Ohio St.3d 356, 2003 Ohio 6453 (2003) (preparation of deed by title agency for its customer, where not prepared or reviewed by an attorney, constituted unauthorized practice of law); *Ex Parte: Charles M Watson, Jr., County Atty. for Greenwood County, Petitioner; In Re: The Unauthorized Practice of Law*, 356 S.C. 432 (S. C. 2003) (when nonlawyer title abstractors examine public records in connection with title search and then render an opinion as to the content of those records in connection with tax foreclosure sale, they are engaged in unauthorized practice of law); *Doe v. McMaster*, 355 S.C. 306, 315-16 (2003) (title company's title search and preparation of title documents for lender, without supervision of attorney, constituted unauthorized practice of law); *State v. Buyers Service Co.*, 292 S.C. 426, 432-33 (S.C. 1987) (preparation of title abstracts by title companies for purchasers of residential real estate without supervision of attorney constituted unauthorized practice of law); *Doe Law Firm v. Richardson*, 636 S.E. 2d 866, 867 (S.C. 2006) (certain title services, including disbursing loan proceeds for a residential refinance or line-of-credit loan, constituted practice of law in South Carolina; court reasoned that "disbursement is an integral step in the closing of a residential refinancing or credit line transaction, which must be conducted under the supervision of an attorney"); *American Abstract and Title Co. v. Rice*, 2004 Ark. LEXIS 401 (Sup. Ct. of Ark. June 17, 2004) (title company acted as settlement and escrow agent during real estate transaction involving class representatives, who alleged that title company engaged in unauthorized practice of law; court certified the matter as a class action); *In re UPL Advisory Opinion 2003-2, 277* Ga. 472 (Ga. 2003) (preparation of "deed of conveyance," i.e., a grant deed or deed to secure debt, and facilitation of the execution of a deed of conveyance, i.e., notarization, constitute the "practice of law," and performance of these functions by anyone other than a licensed Georgia attorney constitutes the unauthorized practice of law); *In re Van Dyke*, 296 B.R. 591 (Bankr. D. Mass. 2003) ("there is a split among the states as to whether just the completion of legal forms constitutes the unauthorized practice of law," but "the majority view [is] that the preparation or filling in of blanks on preprinted forms constitutes the practice of law." Id. at 594-95). *But see Dressel v. Ameribank*, 468 Mich. 557 (2003) ("In general, the completion of standard legal forms that are available to the public does not constitute the practice of law." *Id.* at 568).

Determination of what actions constitute the unauthorized practice of law in real estate transactions is not settled or consistent, and it may be that in New Mexico it is customary for title companies to advise the parties to a real estate closing on certain legal matters and prepare or complete certain form legal documents (such as deeds). But in doing so, such parties generally will be held to the standard of a competent real estate lawyer and may, as in the Barrington case, be liable under various contract and tort theories and state statutes in situations where not advising the parties of the availability of title insurance (or even suggesting that title insurance not be obtained) occurs and a title defect subsequently arises that would have been covered by title insurance. A special American Bar Association "Task Force on the Model Definition of the Practice of Law" reviewed the practice of law in the various states and issued a report and recommendations, dated June 11, 2003, for presentation to the ABA House of Delegates. Among the recommendations was "that every jurisdiction adopt a definition of the practice of law." The ABA Task Force, in connection with its report and recommendations, prepared a proposed definition of the "Practice of Law" ("Model Definition"), which contains the following section:

(e) Any person engaged in the practice of law shall be held to the same standard of care and duty of loyalty to the client independent of whether the person is authorized to practice law in this jurisdiction. With regard to the exceptions and exclusions listed in paragraph (d), if the person providing the services is a nonlawyer, the person shall disclose that fact in writing. In the case of an entity engaged in the practice of law, the liability of the entity is unlimited and the liability of its constituent members is limited to those persons participating in such conduct and those persons who had knowledge of the conduct and failed to take remedial action immediately upon discovery of same.

Reporter's Comment 6: The appellate court in *Barrington* also noted that Fidelity advised Barrington not to obtain a title policy because, "Barrington was protected by the policy issued to Freeze." 172 P.3d at 169. But this is not sound advice. Paragraph 2 of the Conditions and Stipulations of the standard 2006 ALTA Owner's Policy provides that coverage under the Policy continues "only so long as the insured retains an interest in the estate or interest in the Land, or holds an obligation secured by a purchase money Mortgage given by a purchaser from the Insured, or only so long as the Insured shall have liability by reason of warranties in any transfer or conveyance of the Title." (Emphasis added).

Even assuming that Freeze gave a general warranty deed to Barrington (the *Barrington* case does not mention the form of the deed or the purchase price paid by Barrington), without title insurance Barrington would have to first bring an action against Freeze based on breach of the deed warranties as a result of the title defect. Freeze would then tender the claim to Fidelity to defend him against the lawsuit. Because Fidelity admittedly "made a mistake," in failing to discover and disclose the recorded agreement that prevented the use of the property as intended, it would most likely settle the claim. In any event, Fidelity would be responsible for all legal costs and expenses of defending the action, and would also be liable for damages up to the liability amount of the Owner's Policy issued to Freeze.

In other words, it would be possible that Fidelity would have the same liability (or a major portion thereof) as if it had in fact issued a title policy to Barrington, but without the benefit of having obtained any title premium. The only possible good news for Fidelity would be, as noted above, that its liability would not exceed the amount of the insurance under the Freeze policy, which might be less than the damages incurred by Barrington (depending on any appreciation in the value of the property conveyed to Barrington and reflected in the purchase price of the property, and the amount of provable damages incurred by Barrington).

If the conveyance of the property instead was by a special or limited warranty deed, and not by a general warranty deed, Freeze would have covenanted to warrant and defend the title only against claims arising "by, through or under" Freeze, as grantor, and would not have warranted the property against a title defect caused or created by any other party (in which event Barrington would be precluded from any action for breach of the deed covenants against Freeze, which in turn would preclude any action against Fidelity under Owner's Policy previously issued to Freeze).

Also, in many jurisdictions recovery under warranty deed covenants is limited to the consideration the grantor actually received, i.e., the measure of damages for breach of warranty is limited to such an amount; therefore, no title insurance coverage would exist where there is no actual consideration. Even if valid consideration for the deed were established (which is unclear from a reading of the Barrington decision because the amount of the consideration paid for the sale of Lots 8 and 9 by Freeze to Barrington is not stated), Barrington would be required to assert a claim against Freeze for breach of the deed covenants in order to trigger Fidelity's obligation to defend and indemnify under the Owner's Policy obtained by Freeze when he originally bought the lots. Freeze could easily (and understandably) become offended at the prospect of becoming involved in a legal action of indeterminate length, with depositions and interrogatories, filed against him by someone to whom he intended to convey a valuable benefit.

The Reporter for this item was Jack Murray of the Chicago Office of First American Title Insurance Company. The editor has made substantial modifications, so don't blame Jack for typos.

WATERS AND WATER RIGHTS; APPROPRIATION RIGHTS; ELIGIBLE APPLICANTS: A mineral lessee is not considered an agent of the lessor for the purpose of acquiring water rights, unless stipulated in the lease. ***Hydro Resources Corp. v. Gray & Frost, 2007-NMSC-061, ____ N.M. ____, 173 P.3d 749,*** discussed under the heading: "Waters and Water Rights; Appropriation Rights; Mineral Leases."

Under most circumstances, including mining, water rights are not considered appurtenant to land under a lease. ***Hydro Resources Corp. v. Gray & Frost, 2007-NMSC-061, ____ N.M. ____, 173 P.3d 749.***

The two disputing named parties in this case traced their ownership of the disputed water rights to their predecessors-in-interest. Hydro Resources Corporation's ("Hydro") predecessor was Inspiration Development Company ("Inspiration"), and Harris Gray and William Frost's predecessor was the Copper Flat Partnership ("CFP").

On July 15, 1964, Inspiration (lessor) entered into a mineral lease with Corbin Robertson (lessee). On June 9, 1980, Robertson assigned the lease to CFP. On February 17, 1984, CFP drilled wells, thus appropriating underground water, and filed water rights' declarations with the Office of the State Engineer for 6,462 acre-feet of water rights for use at the mill. The Editor understands that New Mexico's appropriation system, which applies both to underground and surface water, confirms in appropriators a priority claim in a water source, so that if the water source depletes, others with lower priority will be required to curtail their use in order to protect the water access of prior appropriators. In a dry state like New Mexico, such rights can have considerable value.

In 1986, CFP ceased mining the claim and the lease terminated, so CFP returned the leasehold interest in the mine and physical improvements to Inspiration. Shortly thereafter, on April 7, 1987, CFP conveyed its water rights to Gray and Frost. Again, the editor assumes that this conveyance meant that Gray and Frost could appropriate from the same underground water source. As they didn't own the land on which the wells were located, Gray and Frost would have to apply to the Engineer for permission to relocate the site of their access to the underground source.

On August 24, 1987, Hydro entered into a mineral lease with Inspiration. The lease gave Hydro "the *right to use* all water rights and all other appurtenances."

On January 8, 2001, Hydro filed a quiet title suit against Gray and Frost in state district court, seeking to quiet title to certain water rights allegedly associated with Hydro's mining claims.

First, Hydro argued that when CFP, a tenant under a mineral lease, obtained the water rights in question, it did so as the agent of the landlord in obtaining the water rights.

Further, Hydro took the alternative position that water rights developed on Inspiration's mill sites were "'appurtenant or otherwise necessarily linked or indispensable to' associated patented and unpatented mining claims." It claimed that appurtance was necessary because otherwise the mining claims could not be worked and the mining rights of those claims that were unpatented would lapse to the federal government. (Some of Hydro's rights were patented, and others were patented.) Thus, once CFP put the wells to use in connection with mills on the leasehold property, the water rights associated with those wells became part of the property rights, and reverted to the lessor when CFP's lease ended.

The Court of Appeals agreed with Hydro on the agency argument. It found that CPR had acted as agent for its lessor in obtaining the rights.

The Supreme Court reversed. It found that CFP was not the landlord's agent in obtaining the water rights: "The default position, absent evidence of a contrary intent, is that *no* agency relationship exists between the parties to a lease." *Id.* ¶ 38

The Supreme Court then moved to the second argument, that the rights necessarily were appurtenant to the property on which they had been used. The court noted that the well established water rights doctrine in New Mexico is that "water rights are separate from the surrounding land and may be owned separately from the land, regardless of necessity." "Water rights that are not appurtenant to land are separate items of property and must be separately conveyed." Consequently, when CFP applied for the water rights to be used in connection with its mining operations under the mineral lease, it obtained those rights in its own capacity, and they did not attach to the lessor's title. They were separately conveyable, and in fact CFP did separately convey them to Gray and Frost. The court noted that the absence of the water rights would not necessarily mean the loss of the federal mining claims, as there were other ways to protect those claims other than continuous operation of a mill site.

The Court, therefore, remanded the case to the district court with instructions to quiet title to the disputed water rights in Gray and Frost.

Comment: Of course, water appropriate rules are state specific, and the "wet" half of the U.S. doesn't even bother with them – following for the most part classic common law rules that view the right to underground water as a part of ownership of the land. Some, in fact, follow the rule that underground water belongs to the party that taps into it, whether a landowner or not.

But in appropriation states, an elaborate statutory scheme, usually administered by a state agency (often the State Engineer) preempts the common law of water rights and, as shown here, severs the rights from the land. The court noted that the New Mexico scheme preserves irrigation rights as part of the land, but not water used for other purposes. As indicated, what this means is that the priority is protected wherever the user taps into the water source.

In most states, water appropriation rights will be viewed as abandoned if they are not put to use continuously, so the Editor assumes that Gray and Frost had already started withdrawing water from the underground source at some other point. The landlord continued to use the wells, possibly without a permit, but if the source depleted, the landlord or its tenants or successors will have to terminate withdrawal in order to permit continued access to water by those with higher priority.

WORDS AND PHRASES; "ACTUAL KNOWLEDGE:" For purposes of construing whether a purchaser of registered title was in "good faith" the presence of electricity poles and use of electricity by a property owner do not prove the property owner had actual knowledge of the location of an easement for purposes of amending the certificate of title to registered land**. *Commonwealth Elec. Co. v. MacCardell, 876 N.E.2d 405 (Mass. 2007)***, discussed under the heading: "Recording Acts; Registration; "Actual Knowledge."

WORDS AND PHRASES; "BUSINESS OR COMMERCIAL USE:" A homeowner's operation of a licensed day care out of her home, caring for up to twelve children daily, constituted a commercial use in violation of a housing development's restrictive covenants prohibiting commercial enterprise, but a facility with fewer children might not. ***Lewis-Levett v. Day, 875 N.E.2d 293 (Ind.App. 2007)***, discussed under the heading: "Servitudes; Restrictive Covenants; Use Restrictions; "No Commercial Use;" Day Care."

ZONING AND LAND USE; "FAIR SHARE" HOUSING; PROCEDURE: STANDING: A developer who seeks a builder's remedy under the *Mt. Laurel* doctrine but is unable to satisfy one of the pre-conditions for such relief, still has standing to continue a *Mt. Laurel* action challenging the constitutionality of a zoning ordinance on the basis that the ordinance does not provide a realistic opportunity for a municipality to meet its fair share housing obligation. ***Oceanport Holding, L.L.C. v. Borough of Oceanport, 398 N.J. Super. 622, 935 A.2d 850 (App. Div. 2007).***

ZONING AND LAND USE; PROCEDURE; "FREEZE" STATUTES: A town's inaction, resulting in constructive approval of landowners' subdivision plans, did not constitute the "final approval" necessary to trigger the statutory eight-year zoning freeze on further zoning actions pertaining to the property. ***Kitras v. Zoning Administrator of Aquinnah, 875 N.E.2d 503 (Mass.App.Ct. 2007)***.

ZONING AND LAND USE; PROCEDURE; STANDING; VARIANCES: Board could override commercial use dimensional requirements when granting comprehensive permit for affordable housing development; flooding to abutter's real estate conferred standing; and, municipal housing authority that owned abutting land has standing as a "person." ***Jepson v. Zoning Board of Appeals of Ipswich, 876 N.E.2d 820, (Mass. 20007).***

YMCA owned slightly more than two acres of land located in Ipswich. Part of the property was zoned "highway business," which allows for commercial components. Jepson and the Ipswich Housing Authority (IHA) owned property abutting and across this street from this property.

The Zoning Board of Appeals of Ipswich (ZBA) granted the YMCA a comprehensive permit, for forty-eight rental units of low and moderate income housing on both properties, and an additional 8,220 square feet of commercial space at its second parcel to be used as a childcare center, bank, and coffee shop. The commercial component of the plan failed to comply with the minimum front setback of fifty feet and the minimum side setback of twenty feet established by local zoning ordinance. The YMCA property also abutted streamways and wetlands, and the ZBA attached conditions regarding drainage and storm water management to the comprehensive permit.

Jepson and the IHA challenged the ZBA's decision to grant the comprehensive permit. The judge granted Jepson standing due to diminution in value of his property, declined to rule on the IHA's standing, and rejected the claim that the ZBA lacked authority to override local zoning requirements in issuing the comprehensive permit. The plaintiffs appealed.

In accordance with its recent decision in *Standerwick v. Zoning Bd. of Appeals of Andover*, the Supreme Judicial Court rejected Jepson's standing based on diminution of land value. *See* 849 N.E.2d 197 (Mass. 2006). The court then reasoned that Jepson qualified for standing under a different rationale. Jepson was a "person aggrieved" because flooding to his property constituted an injury to his property interest, which G.L. c. 40B was intended to protect. Though the YMCA produced experts who determined the project would have no negative impact on the wetlands area that affects Jepson, the court held that

Jepson did not have to produce his own experts to rebut their testimony. Jepson's affidavits and documents from the conservation commission were substantial enough to qualify as "credible evidence to substantiate his allegations."

The court then determined the IHA was a "person" for standing purposes under G.L. c. 40B, § 21. The court ruled that because the IHA actually owns land abutting the proposed development, it qualifies as a "person," even though municipal planning boards generally do not. *See Planning Bd. Of Hingham v. Hingham Campus, LLC,* 780 N.E.2d 902 (Mass. 2003).

Finally, the court ruled that the ZBA did have the authority under G.L. c. 40 B, §§ 20–23 to override local dimensional zoning requirements for commercial use included within an affordable housing development. The court reasoned that the state legislature intended to give zoning boards flexibility to provide relief from exclusionary zoning practices, including allowing commercial components to affordable housing that provide incentives to developers. Standing is granted to both plaintiffs, but the approval of the comprehensive permit by the ZBA was upheld.

ZONING AND LAND USE; VARIANCES; REVIEW OF DENIAL: Without a factual basis, a land use board cannot simply conclude that to grant a variance would be detrimental to the zoning plan or the neighborhood and the board must act liberally when the deviation requested by the variance is *de minimis*. ***Cohen v. Board of Adjustment of the Borough of Rumson, 396 N.J. Super. 608, 935 A.2d 842 (App. Div. 2007).***

An owner of real property in a residential zone proposed razing his then-existing house and constructing a new one. He hired an architect, who submitted plans that only appeared to, but did not conform with, all of the zoning ordinance's requirements. The municipality issued a building permit pursuant to which the home was built. Ultimately, the one nonconformity with the ordinance was a violation of the maximum building coverage allowance; a covered rear porch caused the dwelling to be 293 square feet larger than permitted. The owner sought a variance for that nonconformity. The owner's expert testified that the roof over the porch was an integral part of the house's drainage system, and that it was a material, necessary feature of the house. He concluded that it was not possible to reduce the overall size of the building to cure the almost 300 square feet of excess building coverage. Another expert testified that the porch roof had no visible impact on the neighborhood, as it was only visible to one neighboring house. The owner of that house testified that he had no problem with the offending porch. The municipality's construction official testified that the permit was issued based upon a miscalculation rather than any misrepresentation.

The board rejected the variance application, stating that no basis had been presented to justify the excess building coverage. The owner filed suit to challenge the board decision, arguing that the board ignored his expert's testimony as to the minimal impact of the porch roof and its role in the structure's drainage system. The lower court concluded that the board failed to articulate any reason why the expert witness testimony in support of the owner's variance application was flawed. The court emphasized the *de minimis* nature of the deviation as well as the porch roof's role in the home drainage system. Accordingly, the Court found that the board's ruling was arbitrary, unreasonable, and capricious. The board appealed.

The Appellate Division held that the board of adjustment's denial of variance was arbitrary. It found that the board, without a factual basis, simply concluded that to grant the variance would be detrimental to the zoning plan and the neighborhood. The Court held that the minor variation from the building coverage requirements did not render the structure unlawful under the land use law. While the Court agreed with the lower court that the board's decision was to be set aside, it remanded the application to the board to reconsider the application and make appropriate findings of fact, giving due regard to the testimony of the owner's experts. It disagreed with the lower court's rationale for ordering the variance (i.e., the municipality had previously approved the architect's plans and the building commenced before the parties realized the plans were in error).

ZONING AND LAND USE; USE RESTRICTIONS; RELIGIOUS ACTIVITIES; RLUIPA: Where City's redevelopment plan prohibits church uses in a downtown redevelopment area because state law restricts drinking alcohol in proximity to such churches and the plan calls for an entertainment district with bars and restaurants, the city does not violate the federal RLUIPA law because the City policy is "neutral and applied evenly" to all uses that are not likely to further the municipality's goal of a revitalized downtown. ***The Lighthouse Institute For Evangelism, Inc. v. City of Long Branch, 510 F.3d 253 (3rd Cir. N.J. 2007)***.

A church rented space within a municipality's central commercial district. Six years later, it submitted an application for a zoning permit to use the property as a church. The application was denied because the proposed use was not a permitted use in the zone. The church filed suit challenging the ordinance upon which the denial was based, alleging a violation of the federal free exercise clause of the First Amendment and a violation of the Religious Land Use and Institutionalized Persons Act (RLUIPA).

While the litigation was proceeding, the municipality adopted a Redevelopment Plan that strictly limited the properties within a corridor in which the property was located. The Plan superseded the challenged ordinance. The plan allegedly was established to set up a vibrant and vital downtown community in which restaurants, bars, and clubs were permitted, but churches, schools, or government buildings were not.

Notably, the governing council ultimately concluded that the existence of a church in that zone would compromise its intention that the area be focused on for entertainment and recreation because New Jersey law prohibited the issuance of liquor licenses within two hundred feet of a house of worship. The U.S. District Court held that neither the ordinance nor the plan violated RLUIPA or the Free Exercise Clause of the United States Constitution. The church appealed the entry of summary judgment for the municipality and the denial of its motion for partial summary judgment with respect to its free exercise and RLUIPA claims.

In the appeal, the Court of Appeals made a number of interpretations of RLUIPA. Because that statute is quite remarkable, the editor has elected to set forth salient parts of it here:

a) SUBSTANTIAL BURDENS-

(1) GENERAL RULE-No government shall impose or implement a land use regulation in a manner that imposes a substantial burden on the religious exercise of a person, including a religious assembly or institution, unless the government demonstrates that imposition of the burden on that person, assembly, or institution-

(A) is in furtherance of a compelling governmental interest; and

(B) is the least restrictive means of furthering that compelling governmental interest.

(a) DISCRIMINATION AND EXCLUSION-

(1) EQUAL TERMS-No government shall impose or implement a land use regulation in a manner that treats a religious assembly or institution on less than equal terms with a nonreligious assembly or institution.

(2) NONDISCRIMINATION-No government shall impose or implement a land use regulation that discriminates against any assembly or institution on the basis of religion or religious denomination.

(3) EXCLUSIONS AND LIMITS-No government shall impose or implement a land use regulation that-

(A) totally excludes religious assemblies from a jurisdiction; or

(B) unreasonably limits religious assemblies, institutions, or structures within a jurisdiction.

The District court had held for the City on the claim of discrimination under 2 (b) (2), above, on the grounds, *inter alia*, that if the City has discriminated specially against churches, the church still had the burden to show that the discrimination had a substantial impact on the plaintiff church. The Third Circuit disagreed, holding that the "substantial impact" test did not apply when there was a specific discrimination.

But the Third Circuit disagreed with this interpretation. No substantial burden must result from a discrimination for a claim to arise under the statue.

As to the proving of discrimination, the District Court had held that the plaintiff church is required to show a specific comparator that is not adversely affected by the statute even though it generates the same combination of uses. But the appeals court ruled that the plaintiff need not find a comparator that did exactly the same thing. But it did hold, contrary to the position of the plaintiff, and contrary to Eleventh Circuit authority, that the plaintiff must show a nonreligious comparator not affected by the regulation that presents the same impacts on the governmental regulatory objectives. Thus, for instance, if the regulated conduct is "assemblies," the City could prohibit large religious assemblies but still permit ten member book clubs, if the book clubs don't present the same density issues that are the target of the regulatory concern.

Ultimately, the court concluded that the original zoning ordinance did not focus on plaintiff as a church, but simply as an "assembly hall." In other words, the ostensible regulatory objective to avoid churches that would "squeeze out" purveyors of alcohol could not be viewed as the objective of the ordinance. Since, otherwise, there was not much basis for discriminating against "assemblies" of the sort represented by the church, and still permit restaurant and bar "assemblies," the ordinance was a RUILPA violation. This finding gave the plaintiff some attorney's fees, but otherwise the impact of the ordinance was moot in light of the subsequent redevelopment plan.

The Court found that the municipality's redevelopment plan, which superseded the ordinance, did not violate the equal protection guarantee of RLUIPA given that a church's presence in the redevelopment corridor would hinder the issuance of liquor licenses.

As to the free exercise clause of the First Amendment under the United States Constitution, the Court held that a religious claimant must explain in what way the inability to locate in a specific area by reason of a zoning regulation affects its religious exercise. In the instant matter, the Court found no violation of the clause on account of the redevelopment plan. In fact, the church's minister indicated that he could move four blocks away and still provide services to the impoverished residents of the municipality. Thus, the Court ruled that the redevelopment plan, in preventing religious organizations from locating in a downtown area, was neutral and applied evenly to all uses that were not likely to further the municipality's goal of a revitalized downtown. Therefore, it was not adopted to infringe on religious practices.

The Court remanded the matter to address claims for compensatory damages and attorneys' fees based on the original ordinance's violation of RLUIPA before implementation of the redevelopment plan.

A dissenter, in a lengthy dissenting opinion, strongly challenged the finding that the Plan was valid under RLUIPA. The critical part of the dissent's analysis is that it refused to accept the notion that local government had a legitimate neutral regulatory objective in avoiding the impact of the state law "no alcohol curtilage." In the view of the dissent, the "no alcholol curtilage" was also a government created characteristic, the government can't "bootstrap" a church into an avoidable nuisance by dressing it up with special protections, then using those protections to restrict its activities.

In general, the dissent would abandon any requirement for "comparators." The question to the dissent was whether there is special negative treatment afforded churches. Here, of course, there was. Most other public assemblies do not have the no alcohol curtilage, and so only churches and schools are restricted from the zone. This was not acceptable to the dissent. In fact, it was exactly the conduct, in the view of the dissent, that RLUIPA is supposed to prevent.

Comment 1: It is difficult for the editor to condense a tightly written forty pages of legal analysis into a few paragraphs here. If you are a RLUIPA maven, you should read this one.

It appears that the dissent argues that when a church is disadvantaged in terms of land use rights specifically because it is a Church, that violates the rule in section B(1) above: "No government shall impose or implement a land use regulation in a manner that treats a religious assembly or institution on less than equal terms with a nonreligious assembly or institution."

The editor emphasizes that it is the discrimination, not any adverse burden, that is found offensive. The church was only renting, and could rent space only two blocks away to serve it's congregation. The rules didn't really injure its religious practices in any way.

Comment 2: Churches and bars; bars and churches. They're certainly not compatible, and if government wants to encourage the development of one use, it probably wants to restrict the development of the other use. Certainly it would be able to do this as a matter of general Constitutional law and land use law. But does RLUIPA say that you can't do it in the way things were done here – by excluding churches because another government policy creates a curtilage around them?

Is the answer that "you can't get there from here" – that you can never deny churches the ability to locate where they want on the basis of any characteristic that is unique to churches?

ZONING AND LAND USE; VARIANCES; RELIANCE: Change in position not made in reliance on City plan approval is not a sufficient equitable basis for the issuance of a zoning variance. ***Steamboat Realty, LLC v Zoning Board of Appeal of Boston, 875 N.E.2d 521 (Mass.App.Ct., 2007)***.

Steamboat received a building permit based on plans that reflected no change in the height of the roof line of the building. In the course of renovations, however, Steamboat increased the height of the building. This increase triggered issuance of a notice of violation by the Back Bay Architectural Commission. In response, Steamboat sought a height variance from the zoning board of appeal of Boston (the "ZBA").

The ZBA denied Steamboat's application. On appeal, Steamboat essentially conceded that the property did not meet the codified requirements for the grant of a variance. But Steamboat instead argued that the variance should be granted on equitable principles, with the primary supports for the argument being great expense which Steamboat had undertaken, the potential expense in restoring the roofline, and the "*de minimis*" effect of the changes (which were primarily apparent from behind the building).

The Appellate Court held that a variance was not warranted on equitable grounds. The court observed that financial hardship in-of-itself does not justify a variance. Furthermore, the Court distinguished the present case from past cases in which it was equitable to grant a variance, by highlighting that the City did not cause Steamboat to change its position, that public monies were not involved and that the zoning violation was not a mere technicality, but rather regarding an issue (building height) that the Commission had consistently been strict about. The Appellate Court, applying the trial judge's finding of fact and independently determining the decision of law that those facts required, rejected Steamboat's arguments.