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

July 1 to September 30, 2008

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BANKRUPTCY; MORTGAGES; FORECLOSURE; DEFENSES: Affirmative defenses in foreclosure action were not precluded by bankruptcy order of sale of mortgagee's assets. ***EMC Mtge. Corp v. Atkinson, 888 N.E.2d 456 (Ohio App. 9 Dist. 2008).***

In 1996, Atkinson, Sr. executed a mortgage agreement with UCLC. Apparently a dispute arose immediately, and Atkinson, Sr. never made a payment on the mortgage debt. Less than a year later, UCLC attempted to foreclose. In response Atkinson, Sr. counterclaimed, alleging fraud, negligence, and misrepresentation. During the action, Atkinson, Sr. passed away. UCLC filed bankruptcy, automatically staying the foreclosure action.

On 1999, Atkinson Jr. ("Atkinson") filed a proof of claim against UCLC for an amount in "excess of $25,000," alleging fraud, negligence, and misrepresentation. With that claim pending, in 2000, EMC agreed to purchase UCLC's assets at a "free and clear" bankruptcy sale. EMC allegedly had actual notice of Atkinson Sr.'s counterclaims. In addition to the expected language in the sale order stating that the sale was "free and clear of liens, mortgages, security interests, encumbrances, liabilities, claims or any other interests, whether arising before or after the Petition Date," the sale order also had more specific language about claims:

"[EMC] shall [not] have any liability or responsibility with respect to any Claim against any of the Debotrs [UCLC] or any prior owner of any Mortgage Loan or for any action, or failure to take action, except to the extent [EMC] is found to have liability as a successor under applicable law."

Atkinson became the legal owner of the mortgage property through the probate of his father's estate.

In 2003, EMC filed a foreclosure complaint against Atkinson.

While that foreclosure was pending, in 2005, Atkinson negotiated the outstanding proof of claim with UCLC, which settled for $15,000. Atkinson expressly reserved his claims against EMC.

Atkinson amended his answer and added the affirmative defenses of fraud, coercion, duress, and incapacity.

EMC moved for summary judgment on its complaint and Atkinson's defenses. EMC argued that Atkinson's settlement of the proof of claim and the bankruptcy court's order of sale barred Atkinson's affirmative defenses. It indicated that it was clear that the defenses raised by Atkinson did not fall within the "successor liability" exception. [The court doesn't describe the claims, but appears to accept that characterization.] The trial court granted EMC's motion for summary judgment.

Atkinson appealed, claiming that the trial court erred when it determined that other documents precluded his affirmative defenses.

The Court of Appeals of Ohio reversed the trial court decision and held that: 1) defenses were not barred by settlement agreement between successor and original mortgagee, and 2) the bankruptcy court's order of sale did not preclude assertion of the defenses.

The Court of Appeal, applying federal bankruptcy law as applied by the Third Circuit, first determined that summary judgment was improper because there was a genuine issue of material fact arising from Atkinson's settlement of his claim against UCLC during UCLC's bankruptcy, which stated that it did not in any way represent a full and final settlement as to the claims of Atkinson by and against EMC. The Court found nothing in Atkinson's prior settlement with UCLC that would bar his affirmative defenses in this action. EMC then asserted that *res judicata* barred Atkinson from raising affirmative defenses because the defenses could have been litigated in the bankruptcy action. The Court rejected this claim because EMC provided no authority to support its proposition that the bankruptcy court could have resolved the foreclosure suit filed by UCLC.

Second, the Court held that the bankruptcy court's order of sale did not preclude Atkinson from raising affirmative defenses. The Court used an analogous matter in the Third Circuit, where an entity that was purchasing assets attempted to equate the affirmative defenses raised by the debtor to its own claims to the free and clear provision of the Federal Bankruptcy Code. Section 363(f) provides "The trustee may sell property under subsection (b) or (c) of this section free and clear of any interest in such property of an entity other than the estate." 11 U.S.Code 363(f). The cited precedent, and this court, concluded that this language did not permit sale free and clear of defenses.

What about the separate sale order, which stated categorically that the sale was made free and clear of "claims." The Court concluded that the term "defenses" did not appear specifically in the sale order. It characterized the order as stating that EMC shall have no responsibility for UCLC's "action or inaction." Therefore, the court declined to accept EMC's proffered interpretation that the order restricted Atkinson from raising defenses and held that permitting EMC to purchase UCLCS's assets and preclude Atkinson's assertion of his contractual defenses would enhance the value of the assets at Atkinson's expense which is against public policy. It concluded that to read the sale order so broadly would be inconsistent with the court's authority under the Bankruptcy Code, and that it elected to read it more narrowly.

Thus, the Court concluded that the trial court erred in granting summary judgment on those defenses, and reversed.

Comment: Clearly the court was egregiously misreading the sale order to place the meaning on it that it did. The statement that the sale was free of "claims" – not just claims caused by the action or inaction of UCLC, but all claims – seems grammatically inescapable, but the court makes the reading because it views Section 363 as not permitting sales free of claims raised as foreclosure defenses. So the real news here is the reading of Section 363.

The editor believes that bankruptcy courts in other contexts have read the "free and clear sale" provisions much more broadly than this. It will be interesting to see whether the lender elects to appeal this ruling, to get clarity, or simply to settle up on what appears to be a relatively small matter.

BANKRUPTCY; PREEMPTION; *ROOKER-FELDMAN* DOCTRINE: Alleged fraud raised in state home-foreclosure proceeding could not be raised in federal court because *Rooker-Feldman* doctrine deprived federal district court of jurisdiction. ***Reusser v. Wachovia Bank 525 F3d 855 (9th Cir 2008).***

The Reussers secured a loan from Long Beach Mortgage Company with a home that had been in the family for over 100 years. After the Reussers stopped making payments, Long Beach Mortgage Company assigned its interest to Wachovia Bank, which gave notice to the

Reussers that it would foreclose through Washington Mutual Bank, its loan servicer. The Reussers declared bankruptcy, which stayed the foreclosure action; however, Washington Mutual applied for and received relief from stay under 11 USC §362(a)(3), and foreclosed in January, 2004.

When Reussers didn't relinquish possession, Wachovia, in March, 2004, instituted a forcible entry and detainer (FED) proceeding in Oregon state court to remove the Reussers and take possession. Although the Reussers had served Wachovia with a petition in response, as a result of errors by them and the court, they did not appear at the FED hearing. Wachovia failed to inform the court that it had been served and thereby obtained entry of a default judgment.

The Reussers moved to vacate the default judgment, arguing that their failure to appear was excused by Wachovia's alleged failures to inform the court that it had been served with the petition and to provide notice to the Reussers that Wachovia would seek a default judgment. The Reussers' motion to vacate was denied and their appeal dismissed as mooton the basis that neither Reussers nor Wachovia was in possession of the premises.

The Reussers then sued Wachovia and Washington Mutual in federal court. They claimed that the eviction was wrongful and a violation of 42 USC §1983. They also claimed that the foreclosure violated 11 USC §362 because the order granting relief from stay applied only to Washington Mutual and not Wachovia. They also asserted state-law claims for trespass, trespass to chattels, and false imprisonment.

Washington Mutual and Wachovia moved to dismiss under Fed R Civ P 12(b)(1) and 12(b)(6), asserting that the *Rooker-Feldman* doctrine deprived the court of jurisdiction to rehear the state action claims and that the Reussers were collaterally estopped from challenging Wachovia's reliance on the bankruptcy court's order lifting the automatic stay. The district court dismissed and the Ninth Circuit affirmed.

The *Rooker-Feldman* (*Rooker v Fidelity Trust Co.* (1923) 263 US 413, 68 L Ed 362, 44 S Ct 149; *D.C. Court of Appeals v Feldman* (1983) 460 US 462, 75 L Ed 2d 206, 103 S Ct 1303) doctrine bars a federal district court from exercising subject matter jurisdiction over a suit that is a *de facto* appeal from a state court judgment. Here, the Reussers' claims – that Wachovia failed to provide sufficient notice of its intent to seek a default judgment and then failed to inform the state court that it had been served with a copy of the Reussers' petition contesting the merits of the FED proceeding-had already been litigated in state court and had been rejected on the merits. Therefore, the federal court lacked jurisdiction to hear the §1983 claims, which were properly dismissed.

The Reussers also failed to state a claim under 11 USC §362 because bankruptcy jurisdiction is *in rem.*

Notwithstanding its view of the various fraud claims, the bankruptcy court order granted relief as to enforcement of Wachovia's deed of trust against the Reussers' property; it was immaterial that Wachovia was not specifically named. Moreover, the Reussers' challenge to the bankruptcy court's jurisdiction was waived because the argument could have been, but was not, made to the bankruptcy court.

Reporter's Comment: After a stay has been lifted and a foreclosure has been conducted, an action must be filed to get possession if the trustors have refused to leave, as they did here. Then, all of their defenses may be re-raised, relitigated, and appealed in state court.

It is also worth noting that this decision is almost a rarity in forgiving what might have been the potential error of the loan servicer, rather than the deed of trust holder, being the party seeking relief from the automatic stay. Most federal courts appear to take a much harder line on this issue. *See, e.g., In re Maisel* (Bankr D Mass 2007) 378 BR 19 and *In re Foreclosure Cases* (ND Ohio 2007) 521 F Supp 2d 650. This lender was lucky in having the court hold that the *in rem* feature of bankruptcy moots the personal jurisdiction issue as to creditors. Will that also work for a mortgage assignee who cannot produce a perfect chain of title back to the original loan funder?

Editor's Comment 1: We may see more of the *Roocker-Feldman* doctrine in the interplay of state and federal activities in connection with the ongoing rash of contested foreclosures. For another example of a court dealing with the issue, see ***In re Denaro, 383 B.R. 879 (D. N.J. 2008).***

In *Denaro*, a creditor foreclosed a secured debt in a state foreclosure action. The property sold at this sale for

$401,000 on November 6, 2006. The secured debt, with interest, was about $124,000 higher than the sale price. While the foreclosure was pending, the creditor was simultaneously pursuing an action on the note, and the trial court had found debtor liable on the note on September 15, 2006. Subsequent to the foreclosure, on November 27, 2006, the court in the case on the note entered judgment on the note, crediting the amount bid in by the creditor at the foreclosure sale. [According to the bankruptcy court, the court in this action did not make a finding that the foreclosure price was inadequate, as it had not occurred in September, at the time the hearing occurred.]

In connection with efforts to collect on the judgment, creditor sought an information subpoena and, three months later, Debtor requested an appraisal of the foreclosed property. [We are not informed why the court that authorized the appraisal felt that it was relevant.] The appraisal report found the property as of January, 2007, was worth $750,000, well in excess of the amount of creditor's claim. Note that at that time the debtor didn't own the property. It had been foreclosed upon and purchased by debtor.

Then the debtor filed bankruptcy. The creditor entered an unsecured claim for the $124,000 it claimed it was still owed, and the debtor attempted to challenge the claim on the basis of fact that it appeared that the value of the property significantly exceeded the amount bid at the foreclosure sale.

The creditor responded that *Rooker-Feldman* and principles of *res judicata* and issue preclusion prevented the federal court from undertaking what it argued was an appeal of the state court decision to grant a deficiency claim based upon the results of the foreclosure sale. But the bankruptcy court, claiming that it had studied the record in the state court proceedings, concluded that the issue of whether the property sold at fair market value was never before the various state courts. Thus, the bankruptcy court was free to assess this issue in connection with the ruling on the creditor's claim in bankruptcy.

Ironically, after all that ado, the bankruptcy court upheld the creditor's claim. It concluded that the appraisal, significantly after the foreclosure sale, was a market value appraisal, and did not take into account the "emergency nature" of the foreclosure. It noted that the foreclosure auction was not uncontested – other parties bid against the creditor, and its bid ultimately prevailed, suggesting that the property sold for a "fair foreclosure value."

Although the court refused to apply *Rooker-Feldman* here, it is easy to see how it could be used to preclude bankruptcy court analysis of the validity of a state court deficiency claim, despite argued defects in the claim, if those arguments could have been made in the state court which issued the deficiency judgment.

Editor's Comment 2: The editor is intrigued by Professor Bernhardt's suggestion that the *Reusser* court's second point of analysis, which characterizes bankruptcy proceedings as *in rem*, may preclude arguments about the ownership of secured notes and the mortgages that secure them. But it appears that bankruptcy courts in Ohio and Pennsylvania, as previously reported here, have found lack of jurisdiction to carry out state law foreclosures when the jurisdictional requirements of state law – including clear evidence of ownership of the note – have not been met.

The Reporter for the first item (*Reusser*) was Roger Bernhardt of the Golden Gate Law School, reprinted with permission (albeit edited) from the California CEB Real Property Reporter.

BROKERS; COMMISSION; *QUANTUM MERUIT:* Even where party serving as finder admits that property owners had "no legal or contractual obligation" to pay him for referrals, finder is entitled to make claim based upon *quantum meruit* for "customary" referral fee where finder is an experienced real estate professional and had every reason to anticipate that property owners would pay him for referrals. ***Internacional Realty, Inc., USA Bradenton, LLC, v. Ferrari, 2008 WL 2704643 (W.D. Texas 7/8/08).***

Plaintiffs, who were interested in marketing interests in their apartment holdings to parties seeking to locate 1031 investment monies, had a meeting with Ferrari in which Plaintiffs would pay a free for referrals where parties Ferrari referred would make equity investments.

Subsequently, Ferrari sent invoices to Plaintiff for over $600,000, which Plaintiff paid. Plaintiff later concluded that Ferrarri had done virtually no work and had not worked on a "project by project basis" – although the opinion doesn't make clear what that was.

Plaintiffs sued for a refund of the monies paid and Ferrari counterclaimed for breach of contract and *quantum meruit* for monies he claimed he was owed for additional referrals that had made investments – referrals that he claimed amounted to hundreds of millions of dollars in investments.

Plaintiffs moved to dismiss these counterclaims and the court here ruled on these motions to dismiss. On Ferrari's breach of contract claim, the court found for Plaintiffs because Ferrari admitted, at least thirty times, through pleadings or failure to refute allegations in pleadings that he had no contract.

But on the *quantum meruit* claim, the court concluded that even where there is no legally binding contract, a party providing valuable referrals is entitled to a reasonable compensation for benefits provided if he believed he would be so compensated. The court here concluded that Ferrari, an experienced real estate professional, reasonably could have believed that plaintiffs would compensate him consistent with custom and practice in the industry for finders.

Comment: This is a trial court ruling and there are no findings of fact as to whether any parties who invested in Plaintiffs' properties were in fact Ferrari referrals. That will be decided later.

CONSTITUTIONAL LAW; DUE PROCESS; NOTICE; PROPERTY TAX SALE: In order for a property tax sale to satisfy due process, the Tax Bureau must give thirty days' notice to the person who owns the property at the time of the sale, even if that person is different from the one who owns the property at the commencement of the proceedings. ***Citimortgage, Inc. v. KDR Investments, LLP, 954 A.2d 755 (Pa. Commw. Ct. 2008).***

Neely, a homeowner, could not make her mortgage payments or pay her property taxes. The lender, Citimortgage, foreclosed and purchased the property at a Sheriff's sale on July 13. On July 17 of the same year, before the deed was recorded, the Tax Bureau sent a certified letter to Neely, who was still the owner of record, attempting to notify her that the property would soon be put up for a tax sale. Because Neely had already moved away, and because the letter was addressed to "Neely Tina," the post office returned the letter to the Tax Bureau, unable to forward it.

On September 6, some time after the deed showing the sale to Citimortgage was recorded, the Tax Bureau sent a final notice of the impending tax sale to a Citimortgage office in Texas by regular, not certified, mail. Twelve days after mailing the letter, the Tax Bureau sold the property to a third party at a tax sale. Citimortgage filed objections and exceptions to the tax sale.

This appellate court held that the tax sale violated Citimortgage's due process rights and was thus void. Due process requires that the Tax Bureau strictly comply with the notice requirements under the applicable statute. In this case, the Pennsylvania statute required a full thirty days' notice, by certified mail, to the person who will own the property at the time of the sale, even if that person is not the one who owns (or is on record as owning) the property at the time the Tax Bureau attempts to send its first letter. If the property changes hands (through any kind of transfer) after the Tax Bureau sends the first letter of its intent to hold a tax sale, then the Tax Bureau must begin the process over again, with a new first notice letter and thirty-day waiting period. In emphasizing its point, the court stated: "A property that changes owners one day before a scheduled tax sale must be delisted in order to give the new owner at least 30 days advance notice, by certified mail, of the impending tax sale."

Reporter's Comment: It is interesting to note that there was some communication between the Tax Bureau and the Sheriff, who exchanged delinquency lists prior to the two sales. Apparently, "the Sheriff sometimes collects the delinquent taxes at the time of the foreclosure sale, but he did not do so in this case." If the Sheriff had brought up the issue of the owed taxes at the Sheriff's sale, then Citimortgage would have paid them off then, avoiding the expenses of this lawsuit and the harm to the third party whose purchase of the property at the tax sale was ultimately voided.

CONSTITUTIONAL LAW; DUE PROCESS; TAKINGS; EXACTIONS: In determining whether proportionality exists between the exaction and impact, as required by *Dolan,* courts should inquire first into whether the impact and exaction are related in nature, then whether the exaction in fact will address the impact, and third whether the cost of the exaction to the developer is roughly proportional **in dollars** to the financial measure of the impact on the public. ***B.A.M. Development, L.L.C. v. Salt Lake County, —- P.3d ——, 2008 Utah Lexis 158, 2008 WL 4682267, (10/24/08).***

In connection with Developer's proposed subdivsion project, County required Developer to widen the road outside of the subdivision from 34 feet half width to 40 feet half width. Later the County changed its requirement and demanded 53 feet half width. The developer objected that the additional 13 foot requirement was an unconstitutional exaction.

The lower courts held for the county. The Utah Supreme Court considered whether the lower courts properly applied the "rough proportionality" analysis from *Dolan v. City of Tigard*.

The court noted that "rough proportionality" analysis involved an comparison of two factors, the exaction and the development's impact. In determining whether the two factors are roughly proportionate, the court noted that "proportionate," as used in *Dolan* seemed to mean "equivalent."

In remanding, the Supreme Court instructed the lower court to compare the exaction and the impact by valuing the factors in monetary terms – the cost of the exaction to the developer (cost of land or other requirements) and the cost of the impacts to the county absent the exaction. For an exaction to be lawful (not a taking), the cost imposed on the developer must be "roughly equivalent" to the costs of the impacts to the county absent the exaction.

The court did not provide a clear test for what was "roughly equivalent." It stated that "[t]he proportion of 1 to 1.01 is roughly equivalent, while the proportion of 1 to 3 is not." Further, the court noted that if the cost of the exaction and the cost of the impacts are "about the same, they are roughly equivalent for this purpose." Though it gives no exact ratio as to what is the limit of roughly equivalent, the example laid out by the court and language used to describe appropriate ratios clearly implies that costs of the exaction and impacts must be very close to survive Dolan analysis.

Reporter's Comment: The case is noteworthy, since it appears to require a dollar-for-dollar comparison of the value of the exaction to the burdens of the development on the community.

Editor's Comment: This level of comparison strikes the editor as a useful starting point, but it appears to open the way to all kinds of creating cost accounting by the public agency. The whole idea of *Dolan* was to limit the exaction only to those costs to the public directly associated with the development itself. By making the comparison strictly a dollar comparison, one runs the risk of permitting less direct costs to be loaded into the public agency's side of the equation.

The Supreme Court doesn't make this error. It sets as the first requirement a conclusion that the nature of the exaction and impact are related in nature and whether the exaction addresses the solution to the impact.

The Reporter for this item was Rick Knuth of Jones, Waldo in Salt Lake City. The editor has done his thing.

CONSTRUCTION; CONTRACTORS; HOME-OWNERS WARRANTIES: An election to proceed under the New Home Warranty and Builders Registration Act does not preclude a homeowner from later filing suit, if when making its warranty claim, it was done without full knowledge of the nature of the damage and the contractor had deprived the homeowner of a realistic opportunity to understand the nature and scope of the potential problems facing the homeowner when electing to proceed under the Act. ***Ivashenko v. Katelyn Court Company, Inc., 401 N.J. Super. 99, 949 A.2d 279 (App. Div. 2008); May 30, 2008.***

CONTRACTS; INTEGRATION CLAUSE: An integration clause in a waiver of claims that clearly states that the contract supercedes any other agreements dispels any possible ambiguity as to whether all prior claims are waived, as opposed to those that gave rise to the settlement involving the waiver. ***Daines v. Vincent, 2008 UT 51, 190 P. 3d 169 (Ut. 2008).***

Daines individual agreed to work as agents for an organization attempting to develop surgical centers. The original agreement called for payment of $150,000 and other consideration. Later, however, concern arose that the agent had some conflicts of interest in trying to put together the surgical center developers and the doctors' group that would use the center. So there were further negotiations in which, Daines alleged, it was agreed that Daines would receive some shares of stock in an entity to be formed later and would no longer represent the developers. There was some reference to an "equity position" for Daines in some "term sheets," but later term sheets failed to reference the item. Much more history passed, and ultimately a dispute arose about whether Daines was entitled to compensation, how much and in what form. Daines was making a claim for payment of certain promised monies in connection with a particular real estate deal of interest to the surgical group. Ultimately, the following release was executed.

We, [Daines and an associate], do hereby conditionally release West Valley Surgical Center, LLC or any of its members from any and all liabilities and or claims in connection with services provided by us for the due diligence, acquisition of real estate, or any other services rendered to date for West Valley Surgical Center, or on behalf of its members, for the organization, development and operation of an ambulatory surgical center in the West Valley and any services connected with the same. This release encompasses and satisfies any prior agreements and discussions whether written or verbal by the West Valley Surgical Center, LLC or any of its members.

This release shall be conditioned upon the receipt of $50,000 due and payable from the real estate developer of the West Valley City Surgical Center. In addition, by signing below, we agree that any partial amounts paid against the $50,000 liability either by West Valley Surgical Center, LLC or by The Boyer Company, Developer of the Real Estate for the project for amounts owed us shall become unconditionally released by us upon confirmed receipt of said partial payments."

Daines was paid the $50,000, but alleged that he was owed the stock shares as well. The shares came to be a significant interest in the enterprise, worth more than $4 million. A lawsuit developed. The final entity, WVCS, denied that in fact any equity interest had been promised, and that the $50,000 supporting the release comprehended the total amount owed to Daines, including the original $150,00 promised. Daines argued that the release didn't cover all his compensation from the developer in regard to prior conduct, and that the $150,000 owed had been converted into a right to receive the shares. If WVCS claimed that it had never agreed to grant any shares in lieu of cash, Daines argued, then one of the WVCS principles was guilty of fraud for representing otherwise. Defendants moved for summary judgment against Daines based upon the release language.

The majority of the analysis in the case relates to the determination of alleged ambiguity in a contractual provision. The court took the opportunity to clarify existing Utah authority on contract ambiguity, know as the *Ward* rule.

Ward set forth a two-part test for determining facial ambiguity in a contract. First, "when determining whether a contract is ambiguous, any relevant evidence must be considered." The Ward court was hesitant to allow a judge to determine ambiguity based "solely on the extrinsic evidence of the judge's own linguistic education and experience." For this reason, parties are given the opportunity to set forth "relevant and credible evidence of contrary interpretations." Second, after such evidence is received, "the judge must ensure that the interpretations contended for are reasonably supported by the language of the contract." The court made clear that the Ward rule does not set forth a preference for extrinsic evidence over the language of the contract. "[U]nder *Ward*, a finding of ambiguity after a review of relevant, extrinsic evidence is appropriate only when reasonably supported by the language of the contract." The court noted that it had found ambiguity in previous cases based on: a reading of the contract as a whole; missing terms in a contract; and the parties course of conduct. However, each time ambiguity was found, "the contrary interpretations were reasonably supported by the language of the contract." No ambiguity exists.

The court analyzed prong 1 of the *Ward* test, which determines if the language of a contract is "facially ambiguous." This determination is made by the judge-before permitting recourse to parol evidence.

In summary, the court stated that the two-part *Ward* rule requires that a judge first review relevant and credible extrinsic evidence offered to demonstrate that there is in fact an ambiguity. The rule requires that to go beyond the express language in the contract, the language must be susceptible to "contrary, tenable interpretations." In other words, the *Ward* rule justifies a finding of ambiguity *only if the competing interpretations are reasonably supported by the language of the contract.*

The court then applied the *Ward* test and held that the plain language of the release of "any and all liabilities or claims in connection with services provided" was unambiguous as a matter of law. Because there was no finding of facial ambiguity, "the parties intentions must be determined solely from the language of the contract."

Additionally, the court provided a brief analysis of integrated agreements. The court defined an integrated agreement as "a writing or writings constituting a final expression of one or more terms of an agreement."

The court noted that "extrinsic evidence is not admissible on the question of integration where the contract at issue contains a clear integration clause" and concluded that "a contract is integrated if it contains a clear integration clause." Applying this analysis, the court held that a release that "satisfie[d] any prior agreements and discussions whether written or oral" satisfied the "clear integration clause" standard. It further ruled that all of the defendants were unambiguously released from any liability under the document. The individual liability of the fraud defendant was also released, as the court held that he acted always as a representative of the released entity.

Comment: Obviously there's an important lesson here for attorneys involved in settling claims. If the parties have other outstanding issues, makes sure you've thought through whether you've decided to waive them. Here, the allegations of fraud against an individual who had been acting as an agent of the organization released could not be raised because an earlier waiver absolvedthe organization "and its agents."

DEEDS; DESCRIPTIONS: The property description in a quitclaim deed reliniquishing claims in an alley was sufficient to carry out its purpose notwithstanding the fact that the deed included "Pecan street" as a point of reference , although there was no Pecan street in the vicinity of where the alley at issue was located. The description provided "enough information so that a party familiar with the locality can identify the premises with reasonable certainty" ***Chappell Hill Bank v. Smith, 257 S.W. 3d 320 (Tex.App. 2008).***

A quitclaim deed releasing a portion of an easement stated, in its preamble, that the easement ran from "Pecan Street north to Branham Road." In fact, there was no Pecan Street in the area of the parcels affected by the easement. In fact, there was no Pecan Street in the City. The disputed easement area originally ran from *Cedar Street* north to Branham Road.

The court emphasized that "[t]here is no proof or even a suggestion in the record that in 1959 [the lot owners] all owned property in some other specific tract of land in Washington County. . . In fact it appeared from affidavit evidence that there was no Pecan Street in the city, and the party opposing the deed tendered no proof of any other alley to which the quitclaim deed could apply."

Another part of the same deed identified the area to be relinquished as running from the northwest corner of the lot owned by Joe Knight. It also stated that the easement in question ran "parallel to Main Street" and connected originally to Branham Road. The court indicated that the identification of the overall location and the specification of the lot owned by Joe Knight provided sufficient specificity to identify the easement area in question.

DEEDS; RESERVATIONS; TIMBER RIGHTS: In the absence of clear language manifesting an intent to create perpetual timber rights in New Mexico, there is a presumption *against* perpetual timber interests. The court also held that the omission of the word "forever" after the words "heirs and assigns" was fatal to the claim of perpetual timber rights***. Marrujo v. Sanderson, 2008-NMCA- 112, 191 P.3d 588 (N.Mex. App. 2008).***

The reservation in question stated that grantor, for itself, its heirs and assigns, reserved the rights to timber "eighteen inches in diameter measured eighteen inches above the ground" together with rights of ingress and egress to harvest the timber. Disputes about the continued validity of the reservation had gone on for some time. Grantor argued that the language "heirs and assigns" clearly indicated a perpetual right. Grantee argued that the absence of the language expressing "perpetuity" indicated clearly that only a reasonable period was intended, and that a reasonable period had long since passed.

The appeals court, in concluding that there was no perpetual right, commented that New Mexico's approach is similar to that of other states, which "have concluded that an estate in timber is presumed to be of limited duration, unless the parties provide a clear expression of intent to establish a perpetual fee simple interest." This rule applies whether the timber rights are granted or reserved.

The rationale for this rule is that "[p]erpetual interests in timber constitute extreme burdens, which so severely impair surface owners' use and enjoyment of their property that perpetual interests of this nature should be disfavored."

Similarly, New Mexico courts have held that if an estate in timber is limited to a reasonable period of time – rather than in perpetuity – failure to remove the timber in a timely fashion results in termination of the estate. In the instant case, approximately thirty-seven years had elapsed since the reservation, and the Court determined that this exceeded any "reasonable period of time" to remove the timber. Consequently, the reservation had been terminated.

The court also ruled that several general rules of general construction applicable to deeds were balanced by contrary rules and were insufficient to support the claim of perpetual rights.

The court rejected the argument that a reservation to the grantor's "heirs and assigns" was sufficient to constitute "conclusive proof" of an intent to create perpetual rights. In doing so, the court distinguished another case, followed extensively in other parts of the opinion, "which indicates that the term 'heirs and assigns, forever' would have 'clearly manifest[ed] an intention that the grantor should have a perpetual right to have the timber remain on the land.'" *State ex rel. Okla. Planning & Res. Bd. v. Smith, 317 P.2d 219, 223-24 (Okla.1957). Id.* at 4. The New Mexico court regarded the word "forever" as determinative.

Accordingly, the court affirmed the grant of summary judgment in favor of the landowners.

Reporter's Comment: The New Mexico court held that the word "forever" is determinative in the phrase "heirs and assigns, forever" as distinguished from the phrase "heirs and assigns." Does this distinction counsel the practice of "belt and suspenders" drafting? Or does it merely signify that the court was not going to find perpetual timber rights except on the basis of the most compelling evidence? Would it not have been sufficient if the word "forever" or "perpetual" or a similar word had been used elsewhere in the reservation to refer to the timber rights?

Reporter's Comment 2: New Mexico's rule on perpetual timber interests is the modern rule, and the court reviews cases from other jurisdictions that have also adopted it. It is to be expected that most states will adopt this rule eventually. The rationale for this rule is compelling in light of modern circumstances.

Editor's Comment 1: The narrowness of this issue may justify departure from the general rule that the creation of an estate in a grantee "and heirs and assigns" is the creation of a perpetual estate. Certainly there is a policy issue lurking in the degree to which a timber extraction right affects the surface users. Further, one hopes that significant reserved timber rights would be negotiated by the parties with the assistance of able counsel. In fact, the use of the term "heirs and assigns" suggests that at some point technical advice was sought, if only through selection of a form. Counsel engaged in such transfers have a duty to make themselves aware of the special rules concerning timber reservations. Thus, the rule is not such a "gotcha" as it might appear.

There is, nevertheless the concern that the law has created a situation in which the same words are held to mean one thing in one context and another in a different context. In the view of the editor, law should facilitate, wherever possible, the expectations of the parties freely bargaining, and should not impose surprise policy restrictions.

Editor's Comment 2: Does the same limited construction apply to reserved mineral rights, which in some cases can be equally disruptive of surface usage. If not, why not?

The Reporter for this item was Amanda Sanchez of the New Mexico Bar.

EASEMENTS; PUBLIC PRESCRIPTIVE EASEMENTS; PARTIES: A case alleging a public prescriptive easement must include the relevant local government as a party. As the local government may be liable in inverse condemnation if it participates, it may refuse to do so, invoking the state immunity statute. Consequently, it would be rare that a public prescriptive easement suit could proceed in New Mexico. ***Percha Creek Mining, L.L.C. v. Fust, 144 N.M.569, 189 P.3d 702 (N. Mex. 2008).***

Plaintiffs sued neighboring defendants alleging a public easement by prescription and a claim to declare a road public over "County Road 8082," an existing roadway which apparently wasn't really a county road. The trial court dismissed the claim with prejudice for failure to join the county as an indispensable party because, among other reasons, a successful claim would have imposed obligations upon the county to maintain a public road. If the case went ahead without the county, then the county would later claim the county was not bound by this action, which would be an inefficient and fragmented process. The Court of Appeals affirmed.

The court concluded that New Mexico counties do have a duty to maintain public highways, citing. Section 67-2-2 NMSA 1978, and *Sanchez v. Board of County Commissioners*, 81 N.M. 644, 645, 471 P.2d 678, 679 (Ct. App. 1970) (stating that the duty to maintain public highways belongs to the respective counties). The court stated: "[T]he duty to maintain and repair a public road is not speculative, nor is it a possibility. It is a statutorily required. Consequently, we conclude that the Court could reasonably determine that the County was indispensable because if Defendants were to lose on the merits, the County's interests might be adversely affected."

Sanchez was the first New Mexico appellate decision to suggest, if not actually hold, that the establishment of a public prescriptive easement is tantamount to establishing that a county has the duty to maintain and repair the easement as a public road. In other words, a public prescriptive easement is under the control (to some extent) of the county. A number of legal relationships would follow from that status.

In the instant case, the considerations were more complex. The county had been named as a party, but claimed the county was immune. The Plaintiff stipulated the county out on that basis. Section 42-11-1 NMSA 1978 reads:

"42-11-1. Granting immunity; providing for exceptions The state of New Mexico and its political subdivisions or any of their branches, agencies, departments, boards, commissions, instrumentalities or institutions are granted immunity from and may not be named a defendant in any suit, action, case or legal proceeding involving a claim of title to or interest in real property except as specifically authorized by law."

In *Percha*, the claimant having stipulated the county out and having failed to make detailed arguments, the Court concluded that a declaration of a public prescriptive easement would impact the county, thereby making the county an indispensable party. A court could reasonably conclude the court should dismiss the action instead of proceeding without the county. A court could weigh the county's interests more heavily than the claimant's interests in having a forum in which to litigate.

Apparently, the plaintiff was not interested in imposing maintenance responsibilities on the County, but was interested in the declaration of a public easement to strengthen its case for laying utilities down the roadbed. So it wanted a declaration of private rights. It was caught in paradox – if it sought a private real estate interest, it would have to join the county. But the county was immune from suit in private real estate claims.

Reporter's Comment: As a consequence of the decision, if a county claims immunity and is properly dismissed, it would seem that no public prescriptive easement action can be maintained, a coffin-nail for public prescriptive easements in New Mexico.

In many cases, a party defending against a public prescriptive action would prefer to be subject to a legal relationship with a county as opposed to a legal relationship with some amorphous "public." Some counties might prefer to see the public prescriptive easement established and might not claim immunity.

This leads to the fee simple owner's potential claim of inverse condemnation against the county which, if not dismissed on the basis of immunity, would be part of the consideration.

The reporter for this item was Mike Sutin of the New Mexico Bar. The editor substantially changed the text, however, so blame the editor for any problems.

EASEMENTS; SCOPE; TECHNOLOGICAL ADVANCEMENT DOCTRINE: With respect to wireless telephone equipment, the Technological Advance Doctrine, which permits specific easement uses not expressly provided in the easement, but for which technological developments have "further[ed] the particular purpose for which the easement is granted," applies to easements granted with general language permitting "transmission and distributing lines consisting of variable numbers of wires and all necessary and desirable appurtenances." ***Centerpoint v. Bluebonnet, ___ S.W.3d ___, 2008 WL 2930206 (Tex.App.-Hous. (1 Dist.) Jul 31, 2008).***

In 1929, an express utility easement was granted to Houston Lighting & Power Company over property located in Houston. The granting language provided for "a right-of-way or easement for electric transmission and distributing lines consisting of variable numbers of wires and all necessary and desirable appurtenances (including towers or poles made of wood, metal or other materials, telephone and telegraph wires, props and guys)."

CenterPoint, as successor to Houston Lighting & Power, granted SprintCom, Inc. permission to install wireless telecommunications equipment within the easement. Bluebonnet and Petro-Guard, as owners of the servient estate, filed suit against CenterPoint seeking damages, injunctive relief, and attorneys fees, arguing that the wireless equipment exceeded the scope of CenterPoint's easement. The trial court held that the easement foreclosed installation of Sprint's wireless communications equipment. The judgment: "(1) enjoined CenterPoint and Sprint from using CenterPoint's easement for wireless communication; (2) required that Sprint remove its equipment from the property; and (3) awarded Bluebonnet and Petro-Guard damages, interest, and costs against both CenterPoint and Sprint and attorney's fees against CenterPoint." CenterPoint and Sprint appealed.

When analyzing the scope of the easement, Texas Court of Appeals first outlined the general rule that the scope of a particular interest conveyed depends upon the intent of the parties. Specifically, the court cited the Restatement (Third) of Property for the proposition that "an easement 'should be interpreted to give effect to the intention of the parties ascertained from the language used in the instrument, or the circumstances surrounding the creation of the servitude, and to carry out the purpose for which it was created.'" In addition, the "manner, frequency, and intensity of easement may change to take advantage of technological advances, but only for purposes for which [the] easement was created."

In *Marcus Cable Assocs. v. Krohn*, 90 S.W.3d 697, the Texas Supreme Court "construed [a] utility easement as limited to the purpose of conveying electricity by demonstrating that settled law had interpreted the terms 'electric transmission' and 'electric distribution' as referring exclusively to conveyances of electricity," and therefore declined to permit a use that went beyond conveying electricity. However, in the case at bar, the court distinguished *Marcus Cable* in that the language in the easement in that case was much narrower.

Analyzing the plain terms of the easement in this case, the court held that the terms were "amply sufficient to encompass use of CenterPoint's easement for Sprint's cellular transmission lines and equipment." Specifically, the easement granted a right-of-way for "all necessary and desirable appurtenances," which included (i) towers, (ii) poles made of wood, metal, or other materials, (iii) telephone and telegraph wires, and (iv) props and guys. In addition, only in cases where ambiguity exists will a court consider terms not present in the easement, which was not applicable here.

With respect to CenterPoint and Sprint's argument that the technological advancement doctrine applies to permit the installations of wireless telephone transmission and equipment, despite the easement's language only addressing "telephone and telegraph wires," the court noted that the plain terms of the easement "reflect[ed] not only electrical transmission as a purpose of the easement, but also telephone and telegraph transmission as a purpose of the easement." Because an easement properly encompasses technological developments that "further the particular purpose for which the easement is granted," the court took the opportunity in this case to provide "an appropriate application of the doctrine of technological advancement or development," in holding that "a holder of an easement granted in 1940 for the purpose of telephone transmission could properly attach transmitters to its poles for cellular telephone transmissions unless that use would interfere unreasonably with the servient estate."

Based on the foregoing analysis, the court reversed the judgment of the trial court, holding "that the express terms of the CenterPoint easement encompass installation and use of cellular transmission within the easement, and that CenterPoint did not exceed the scope of the easement in assigning those rights to Sprint."

Comment 1: Although the editor has never seen the "technological advancement doctrine" described with that title, it certainly is the case that scope **express** easements can grow to fit changes in the social and technological conditions in which the property exists in the decades following the easement. The parties to the original easement, if asked, almost certainly would have agreed that this was their intent when they created a permanent easement in a changing world. If they wouldn't have agreed, they should have.

Comment 2: The editor checked for any mention of "technological advancement doctrine" in his favorite source for easement law, Bruce and Ely, The Law of Easements and Licenses in Land, now published by West. He found footnote 7 in section 8.3 that catalogues the cases involving changes to accommodate new technology. Clearly the concept is well established, but no mention of a specific "doctrine." Maybe it's time for one.

Comment 3: But coining terms like "technological advancement doctrine" can be very misleading. The fundamental question has to be: is this the deal that the parties originally made? In other words, did the party acquiring the easement acquire this right, which of course may have considerable value? As indicated, the editor is of the view that the dominant tenant in the instant case bought the right to transfer telecommunications data within the easement area, and this would include wireless transmission facilities. But the editor would strictly construe the technological advancement to changes consistent with the original nature of the right.

For this reason, the editor is critical of cases, outlined in Section 8.5 of Bruce and Ely, that appear to take the position that laying of fiber optic cable for general telecommunications purposes in railroad rights of way is not a surcharge of the original easements because there is no injury to the servient tenement. The question of "injury," – interference with the servient use – is really beside the point. In the editor's view, telecommunications transmission ain't the same as driving a train. The original dominant tenants – the railroads – didn't buy such rights, and they didn't acquire the fee, and shouldn't be able to profit at the expense of the servient owners by transferring them to a telecom company. If there's a public purpose here, let the government clothe the telecom companies with eminent domain rights (as it did the railroads) and let the companies go out and get their line rights from the property owners. But that view is just the editors (and a few courts). Progress often washes over the editor like waves over granite. He doesn't even own a Blackberry and rarely sends a text message.

EMINENT DOMAIN; INVERSE CONDEMNATION; ACCESS: Although an inverse condemnation may lie for partial but material obstruction of access to a public highway, no damages will lie for alteration of traffic patterns on the highway, even though the net effect of access to landowner's premises is effectively the same. ***State v. Dunn, 888 N.E.2d 858 (Ind.App. 2008).***

Dunn owned a hotel property that had access, via a service road, to and from the northbound and southbound lanes of Green River Road. The State elected to restrict access to Green River Road and erected a concrete median in its center, thereby preventing southbound traffic from making left turns into the service road entrance to the property. Without the median, southbound traffic would cross over five lanes of northbound traffic to turn onto the service road. Following the change, southbound traffic had to follow a circuitous route to reach the service road.

Dunn filed an inverse condemnation action against the State, claiming that installation of the median completely eliminated access to the property from the southbound lane of Green River Road, thereby substantially and materially impairing vehicular access to the property so as to constitute a taking of property without just compensation.

The State contended that Dunn was not entitled to compensation as a matter of law because the State installed the median under its police powers and it does not constitute a compensable taking. Both parties filed motions for summary judgments. The trial court held for Dunn, finding that a taking had occurred. A jury awarded damages in the amount of $3,650,000, and the trial court awarded an additional $1,049,600 in prejudgment interest, $109 in costs, and $25,000 in attorneys' fees. On appeal, the Court of Appeals of Indiana reversed, holding that the median affected traffic flow, rather than ingress and egress, and therefore did not constitute a compensable taking.

The case was decided under the Indiana Code provision that allows an inverse condemnation claim where a person's property has been requisitioned for public use without the procedures of eminent domain.

The threshold question in such a claim is whether the plaintiff landowner has a property interest in the property that has been acquired by the State. As defined in *State v. Ensley,* 164 N.E.2d, 348-49 (1960), the leading case on the issue, "Property in its legal sense means a valuable right or interest in something rather than the thing itself, and is the right to possess, use and dispose of that something in such a manner as is not inconsistent with the law." This right includes a right of ingress and egress.

Although a property owner has an easement of ingress and egress in an abutting public highway that cannot be taken without compensation, the Indiana Supreme Court held that a taking does "occur where ingress and egress is made more circuitous and difficult" because there is no property right to the free flow of traffic past a property. *Town Council of New Hampshire v. Parker,* 726 N.E.2d 1217 (Ind.2000). Where there has been an interference with the right of ingress and egress itself, a claim is compensable if that right has been "substantially or materially interfered with or taken away." It is insufficient that state action created a partial limitation or obstruction.

Based on this holding, claims are distinguished into two types: those alleging damages resulting from an alteration in traffic flow do not result in a cognizable claim, while those alleging interference with the right to ingress and egress may result in a compensable claim if such interference is substantial or material.

Here, Dunn's claim fell within the first line of cases. The court expressly rejected Dunn's claim that the degree of damages suffered by the business is relevant to determination of which type of claim he is making. In essence, it concluded, Dunn was claiming a right to the free flow of traffic to his property. This, as noted, was not a protected right.

Comment: This is the first time the editor has encountered the stated distinction between traffic flow and actual access to property. Thus, the editor has not thought before about the question of whether the obstruction of traffic flow ought to be compensable as a taking of access if the net effect is to render the business operations on plaintiff's property significantly less valuable.

The editor is symphathetic with the notion that "the line must be drawn somewhere" and that it is quite difficult to judge the net effect of traffic flow modifications on access, and consequently on value. For some purposes, elimination of cars crossing five lanes of traffic to reach one's premises might render the premises more valuable.

In any event, compensation for partial interference with access already is an uphill argument, and the editor isn't surprised that parallel arguments are blocked completely.

EMINENT DOMAIN; PROCEDURE: According to New Jersey statutes, once a property owner withdraws all or part of a condemning authority's deposit from the court, the property owner is barred from challenging the validity of the condemnation, but this does not mean that the property is no longer entitled to argue that the proper valuation date is when the declaration of taking was filed and not the date of the condemnation action. ***Township of Piscataway v. South Washington Avenue, LLC, 400 N.J. Super. 358, 947 A.2d 663 (App. Div. 2008).***

FIDUCIARIES; SALES; JUDICIAL CONFIRMATION: Although parties who are interested in acquiring property being sold at a fiduciary sale have no standing to demand notice and opportunity to participate in the judicial process by which the court approves the sale (in this case, to another bidder, which was also the listing broker), such competing bidders nevertheless have standing to bring a lawsuit alleging a fraudulent scheme to conceal from the court approving the sale critical information about the buyer's status as listing broker. In such lawsuit, the fact that the sale was approved by a court will not conclusively establish that it was a fair and reasonable sale. ***Burke v. Seat Point Realtors, 400 N.J. super 389, 947 A.2d 686 (App. Div. 2008).***

A landowner had become incapacitated and a guardian, landowner's long time friend, was appointed to look after his affairs. Landowner owned property near the beach that apparently had not been occupied in some time and was in need of repairs, but had substantial value.

Guardian listed the property with Sea Point, a real estate brokerage company, and Sea Point got a lot of "action" on the property. Ultimately, guardian submitted a proposal to the probate court that the property be sold to a principal of Sea Point, who was the listing broker for cash, and that another, higher, offer, contingent on financing, be rejected. The submission to the court did not highlight the fact that the property was being sold to the listing broker, although a line in the lengthy, single spaced sale agreement did so disclose.

Three other parties who were interested in buying the property later brought suit for breach of contract and tortious interference against the guardian. The alleged that the brokers had deliberately discouraged the bidders from actively bidding to buy the property by emphasizing problems with the property and not disclosing that they intended to buy it for themselves. The trial court found that the bidders never had a contractual relationship with the guardian, and dismissed the breach of contract claim.

As to the tort claim, the trial court also dismissed, in part on the grounds that the bidders had no standing to participate in the Probate Court proceeding and that that court's determination that the sale to the realtors was not a breach of the fiduciary's responsibilities was conclusive.

The Appellate Division affirmed the finding on the contract claim, but reversed the dismissal of the tort suit, concluding that the fact that the bidders had no right to receive notice of the Probate Court proceeding didn't mean that they couldn't challenge the behavior of the guardian in that proceeding. Further, the court held that the guardian's submission to the Probate Court did not adequately disclose the fact that the buyer was the listing broker, and noted that such disclosure might have triggered greater scrutiny by the Probate Court judge, who affirmed the sale without a hearing.

The appellate court noted that it is not uncommon to give notice of such sales to competing bidders, even though not required, specifically to avoid disputes of the nature that occurred here.

Comment 1: The editor finds this case interesting because of how far the court goes here to honor the complaints of the competing bidders notwithstanding probate court approval of the sale, particularly when there apparently were four other offers produced. Although there apparently was no evidence alleged to show collusion between the guardian and the brokers, other than the non-disclosure of the relationship of the buyer to the listing broker, the court noted that indicia of fraud often aren't discovered until discovery is carried out.

Clearly, in the editor's view, the court "smelled a rat" here. Note that it isn't even clear that the three bidders who brought this suit actually all submitted formal purchase offers.

Comment 2: As we move into a period in which many parties will be dealing with distressed properties in many contexts, and there will be jockeying for position on the part of scavengers, it is noteworthy how broad the New Jersey court here opens the door for challenges based upon fiduciary violations. The same rules that apply to the guardian here conceivably could apply, for instance, to "sweetheart" deals cut between real estate companies and receivers.

An assuming assignee is not obligated to reimburse the original tenant's guarantor for expenses guarantor incurred pursuant to the guarantee agreement where there is no evidence that the assignee knew of the guaranty when it agreed to assume the original tenant's obligations under a lease. Reimbursement is permitted neither not by way of a contractual relationship nor by way of equitable subrogation. ***Feigenbaum v. Guaracini, 402 N.J. Super. 7, 952 A.2d 511 (App. Div. 2008); July 29, 2008.,*** discussed under the heading: "Landlord/Tenant; Guaranties; Equitable Subrogation."

HOMESTEAD; PARTNERSHIP PROPERTY: Property that mortgagee sought to foreclose was partnership property, such that no homestead protection attached thereto, notwithstanding evidence that the deed to the property was in the owners' individual names and that each of the them lived on the property at various times. ***Siller v. LPP Mortg., Ltd., 2008 WL 2181937 (Tex.App.-San Antonio May 28, 2008) (not yet released for publication).***

The Partners emphasized testimony that, although the property was used in the partnership business operations, they intended the property to be their homestead and not partnership property. The argued, that, because the validity of a deed of trust is determined at the time it was executed, the court should not consider evidence of acts or statements subsequent to 1981 when the deed of trust was executed.

The court disagreed. It noted that the partnership had represented to taxing authorities that the property was a partnership asset; property taxes were paid from the partnership checking account; the partners represented to the bankruptcy court that the property was partnership property; and one of them signed a letter stating that the property had always been partnership property.

INSURANCE; TERRORISM INSURANCE: 1989 ground lease requiring standard extended coverage insurance does not allow ground tenant obtaining renewal policy in 2003 to purchase coverage that excludes the risk of terrorism.1989 ground lease requiring standard extended coverage insurance does not allow ground tenant obtaining renewal policy in 2003 to purchase coverage that excludes the risk of terrorism**. *TAG 380 v. ComMet 380, 890 N.E.2d 195 (New York 2008*).

TAG's 25 year ground lease with its lessor ComMet for a building at 380 Madison Avenue in New York, executed in 1989, required it to maintain insurance against all risks "included under the standard Extended Coverage Endorsement as presently adopted". In 2003, when TAG's old insurance policy expired, it purchased a new policy, which specifically excluded terrorism. (This new policy also appeared to undervalue the building, but TAG had privately purchased an additional policy that appears to have covered the full value of the property and did not exclude terrorism; why this was not disclosed to the ground lessor is not explained in the decision.

Upon learning of the apparent insurance shortfall, ComMet sent a notice of default to TAG. TAG responded by filing this action for declaratory relief as to its insurance obligations (a "Yellowstone" injunction in New York). Supreme Court (the trial court) held that TAG was in breach for lacking terrorism coverage, but the Appellate Division reversed and held that TAG had no such duty. However, the Court of Appeals agreed with the trial court, and held that the insurance TAG had obtained violated state insurance law as well as its obligations under its ground lease.

In 1989, when the ground lease was executed, the insurance coverage that was required under it did not exclude terrorism. The replacement policy that TAG ostensibly obtained (i.e., the one known to ComMet) clearly did exclude that risk, and therefore violated the terms of the lease.

Furthermore, New York Insurance Law §3404 prohibits the issuance of policies that exclude particular risks that are otherwise included in a standard policy. (And the Superintendent of Insurance has declared that terrorism exclusions are against the state's public policy and are therefore prohibited.)

Because ComMet had not been informed as to the additional coverage that TAG had purchased, ComMet was entitled under the lease to purchase such coverage itself and to recover that cost as damages from TAG, as well as attorney's fees.

(In a footnote, the court mentioned that the trial court had also held that ComMet was obliged – under its mortgage with GMAC Commercial Mortgage Corp. – to provide such insurance coverage itself pursuant to its loan agreement. This holding apparently was not further appealed.)

Comment 1: The case turns in large part on the definition of "fire and extended coverage insurance" as described in New York insurance law. That law requires that when a fire insurance policy must contain no less than the coverage set forth in the statutory standard form policy, and that "if a policy contains a less favorable term, it is enforceable as if it conformed with the statutory standard. The court here did not attempt to read the policy obtained by TAG as necessarily including terrorist coverage, since it specifically and categorically precluded such coverage. The court simply held that such a fire policy was illegal in New York.

It was not necessary for the court to redefine the insurance provided under the policy because it also concluded that TAG had not satisfied the lease provisions requiring coverage equivalent to that provided by a fire and extended coverage policy as such policy existed at the time of the execution of the lease. Since terrorism was not excluded at the time of lease execution, a policy that excluded terrorism did not satisfy the insurance requirement of the lease, and therefore landlord was justified in buying substitute insurance (which it did) and charging the cost to the tenant.

Comment 2: The editor flagged this case in part because of the notion that New York has held insurance exclusion of terrorism coverage invalid as against state policy. This happened after the operative facts of this case, but obviously in the future will render moot arguments about whether the fire and extended coverage required by the policy can exclude fire or other casualties caused by terrorism.

Also see: Omni Berkshire Corp. v. Wells Fargo Bank, N.A., 02 Civ. 7378 (S. D. N.Y. 2/25/04) (the DIRT DD for 12/13/04). The court there first ruled that a requirement in mortgage instrument that mortgagor acquire all risk" policy does not obligate the mortgagor to acquire all of the coverage available under an "all risk" policy at the time of the mortgage, but only to acquire insurance generally regarded as the equivalent of the "all risk" policy as traded in the marketplace at the time for acquisition of the insurance coverage. But the court took away the mortgagor's victory by then holding that the mortgagee could require the mortgagor to obtain terrorism insurance under the provision requiring mortgagor to acquire such other insurance as lender "reasonably may request." Requirement for terrorism coverage was not unreasonable, despite the fact that the $300,000 annual cost for that item alone exceeded the total insurance budget from prior years.

INSURANCE; MORTGAGES; FORECLOSURE: Under standard mortgage clause providing that mortgagee cannot cancel mortgagee in the event of "increase in hazard, change of ownership, or foreclosure" not known to mortgagee and requiring mortgagee to give insurer notice of "increase in hazard," the fact that a foreclosure has been initiated is an "increase in hazard" and if the mortgagee fails to notify the insurer, the insurer may refuse to cover mortgagee's loss caused to damages due to fire while foreclosure is still pending. ***U.S. Bank, N.A. v. Tennessee Farmers Mut. Ins. Co., 2007 Westlaw 4463959 (12/27/07) (appeal granted 5/27/08)***, discussed under the heading: "Mortgages; Insurance; Cancellation."

LANDLORD/TENANT; ASSIGNMENT: Despite a clause providing that there can be no assignment without the landlord's written consent and providing further that payment of rent shall not be a waiver of this prohibition, an occupant of the premises who pays rent for 18 months with the knowledge and consent of landlord's agent may become an assignee of the lease and recover against the landlord for damages to its goods due to negligent maintenance of common areas. In the alternative, tenant may become a month to month tenant or even a licensee of the original tenant, and in either case be able to recover. ***La Belle Epoque, LLC v. Old Europe Antique Manor, LLC., 4489273 (Md. 10/8/08).***

Landlord leased the upper level of its property to LBE and the lower level to VFA. VFA, which held a five year lease, was owned by a French national, but his sole employee operated the business. The French owner, however, signed the rent checks.

VFA's lease contained a relatively strict restriction on assignments (Maryland case law, like the majority of jurisdictions, upholds the validity of a landlord's right to withhold consent to assignments for any reason.) This particular restriction stated that acceptance of rent by the landlord after an attempted assignment would not be deemed consent to the assignment. The landlord's approval was required to be in writing after notice to the Landlord. The Maryland Statute of Frauds required that lease assignments also be in writing.

About a year into the five year lease, the employee who had been managing the VFA operation made a deal with the French owner that she would take over the business. She paid the French owner $10,000 for the privilege, and he removed his merchandise and she installed her own. She changed the name of the business to Old Europe Antique Manor (Tenant), but for some time after taking over left the VFA sign in front of the store. According to the Employee, she notified both Landlord's agent (the notice address in the lease) and Landlord that she was taking over the store and that the original owner didn't want it any more. She claimed in court that the agent told her that this would be no problem.

For the next 17 months, the Employee paid the rent, most often using checks drawn on Old Europe. The manager, however, continued to address the rental bills to the original owner/assignor.

Things were at this stage when a calamity occurred. The upper level tenant, LBE, had been permitting a large accumulation of debris to develop in the common area outside its premises. Tenant (lower level) complained of this to the manager, but nothing was done. Then an unusually heavy storm hit, and the debris collected snow and directed water and snow runoff in such a way that Tenant's lower level premises were flooded, damaging her inventory and premises to the extent of over $300,000. Tenant was forced to close. Thereafter, Landlord seemed to be willing to take responsibility for the repairs, but ultimately concluded that it would not reimburse Tenant for her injuries because she was not a lawful assignee.

A trial court agreed, indicating that it saw no evidence that Tenant was anything but a trespasser. The duty of cared owed to trespassers, it concluded, was not breached. Summary judgment for Landlord.

On appeal: *Held: Reversed.*

Agreeing with the lower appeals court, the Maryland Court of Appeals court here concluded that Tenant should recover, and took a rather comprehensive approach to analyzing Tenant's status.

The court first held that there was a triable issue of fact as to whether Tenant was indeed a valid assignee. Although the lease stated that acceptance of rent was not waiver to the right to object to an assignment, the court noted that the 17 months of acceptance coupled with notice of Tenant's status of assignee of the original tenant (as Tenant alleged) could constitute waiver of its right to require express notice and written consent. As to the Statute of Frauds, the court noted that Maryland law states that a contract that arises out of "operation of law" does not have to comply with the Statute of Frauds, and that the many months of Tenant's occupancy of the premises and payment of rent with VFA's knowledge and approval made this assignment one by operation of law.

In a somewhat puzzling characterization of the situation, the court talked of the Landlord's implicitly "surrendering" the original lease. (Of course, normally no surrender – no novation – is necessary for an assignment to occur. The Landlord can look to both assignor and assignee for performance of the lease covenants.)

"Intent is a key inquiry in this case. The trier of fact must determine whether [Landlord and VFA] intended to surrender the Lease and/or whether [Landlord] intended to accept Ole Europe as an assignee under the lease, and whether [Landlord], by its actions, waived the requirements of the Lease and Statute of Frauds."

The court went on to conclude that even if Tenant was not a valid assignee, then most likely it acquired a "common law tenancy" (month to month) in the premises. This is what the lower appeals court had concluded. In a footnote, the court noted that even if there were no common law tenancy, tenant could be regarded as a licensee of the original tenant, VFA, and still entitled to the standard of care owed to a tenant.

Once Tenant's status was to be resolved, the court had no difficulty concluding that the alleged facts demonstrated a breach on the part of the Landlord of a duty owed to a tenant, as the Landlord allegedly had actual notice of a hazardous accumulation of debris in the common area.

Comment 1: The editor agrees with the outcome, but is puzzled with the analysis on a number of levels.

First, of course, is the suggestion that there ought to be, and might be, a surrender of the original lease. It is hard to where the court gets this conclusion. The first tenant never contacted the landlord to ask for a surrender and the new Tenant never requested one. A surrender is not a necessary prerequisite for a valid assignment.

The Editor further is puzzled by the court's discussion of the application of the Statute of Frauds. Surely, as between the original tenant, VFA, and the current tenant, part performance had long since nullified the impact of the Statute of Frauds. The old tenant had removed its things and the new tenant had paid $10,000 in cash and then paid rent for 17 months on the understanding that an assignment had occurred. The court characterizes this transfer as an assignment "by operation of law." Well, OK. That's not the Editor's understanding of this concept, but it nevertheless works.

Comment 2: The court clearly is uncomfortable with characterizing Tenant as an assignee, since it considers two alternative formulations: Tenant as a "common law tenant" and Tenant as a "licensee" of VFA. Both work, of course, but it is difficult for the Editor to see why either is necessary. In the Editor's understanding, a lease assignment is valid even in violation of an anti-assignment clause unless and until the landlord is able to declare it void and enjoin further possession. See Friedman on Leases (Randolph Edition) Section 7:3.5.

LANDLORD/TENANT; EVICTION; EVICTION PROTECTION STATUTE; "TENANT:" Tenant who hds signed a lease but never received possession before landlord repudiated the lease is not a "tenant" entitled to statutory remedies available to tenants, precluding emergency of possessory action. ***Olympus Properties, LLC v. Plotzker, 888 N.E.2d 334 (Ind.App.2008).***

Plotzker was a student at Indiana University. He leased apartment 311 in a building managed by Olympus, from August 1, 2006 to August 1, 2007. Plotzker sublet the apartment to John Schwartz from December 2006 until the end of the lease on August 1, 2007, because Plotzker went to study overseas. Also, in December 2006, Plotzker agreed to lease apartment 306 in the Mercury Building from August 14, 2007 (when her would return to campus) until August 5, 2008. On August 1, 2007, when the leasing agent conducted a move-out inspection for apartment 311, he determined the apartment to be in an unsanitary condition, with some of Plotzker's items left behind. Olympus determined that this constituted a hold-over and considered Plotzker in breach of his lease for apartment 311.

On August 2, 2007, Olympus notified Plotzker that it was repudiating the lease for apartment 306 because Olympus considered Plotzker to be in breach of his apartment 311 lease. On August 10, 2007 Plotzker filed a complaint and a motion for emergency possessory order in small claims court as provided by the Indiana eviction protection statute. This statute confers jurisdiction on small claims courts to issue injunctions to prevent wrongful eviction and authorizes the awarding of attorney's fees. The small claims court ordered Olympus to give possession of apartment 306 to Plotzker. Olympus appealed, raising three issues: 1) whether small claims court had subject matter jurisdiction over the case; 2) whether small claims court erred by awarding injunctive relief; and 3) whether small claims court erred by awarding Plotzker attorney fees.

Note that the case did not involve an appeal about whether the repudiation of apartment 306 was wrongful. Apparently the landlord accepted the lower court's determination that it was.

The definition of "tenant" that applies to emergency possessory orders is found in Indiana Code Section 32-31-3-10, which defines "tenant" as "an individual who occupies a rental unit: (1) for residential purposes; (2) with the landlord's consent; and (3) for consideration that is agreed upon by both parties." Under this definition Plotzker was not a tenant of apartment 306 because he never occupied that apartment. Plotzker argued he was a tenant under the holding of *Starks v. Village Green Apartments*, 854 N.E.2d 441 (Ind.Ct.App.2006), in which the fathers of the occupants were determined not to be tenants because the court construed the term "to occupy" in a literal physical sense. Here, Court interpreted the term "to occupy" to mean "to take or hold possession or control of."

The Appeals Court determined that Plotzker was not a tenant because he never had possession of or control over apartment 306, and thus was not entitled to the statutory remedies of a tenant. However, he was entitled to remedies available under contract law for Olympus's breach of the lease.

In regard to injunctive relief, the small claims relied on Chapter/Section 31-31-6, which governs emergency possessory orders. The Court held that this provision granted the small claims court jurisdiction to resolve the case according to contract law. Therefore, the appeals court remanded for the court to consider what damages, if any, Plotzker had suffered because of Olympus' wrongful breach of the contract.

The small claims court had awarded Plotzker $7,505 in attorney fees pursuant to the eviction protection statute. This section allows courts to award attorney fees if a tenant prevails in an action against a landlord. The Court held that the small claims court incorrectly applied the provision because Plotzker was not a tenant of apartment 306. "Thus, an award of attorney fees is not allowable in the absence of a statute, agreement, or stipulation authorizing such an award." The Court therefore remanded to the small claims court to determine whether there is a basis other than the landlord-tenant statutes for awarding attorney fees to Plotzker.

In sum, the small claims court had jurisdiction over the matter. However, because Plotzker was not a tenant of apartment 306, the court could not award injunctive relief or attorney fees pursuant to the landlord-tenant statutes. Thus, the Court remanded for a determination of damages, if any, for Plotzker and whether he was entitled to attorney fees.

LANDLORD/TENANT; GUARANTIES; EQUITABLE SUBROGATION: An assuming assignee is not obligated to reimburse the original tenant's guarantor for expenses guarantor incurred pursuant to the guarantee agreement where there is no evidence that the assignee knew of the guaranty when it agreed to assume the original tenant's obligations under a lease. Reimbursement is permitted neither not by way of a contractual relationship nor by way of equitable subrogation. ***Feigenbaum v. Guaracini, 402 N.J. Super. 7, 952 A.2d 511 (App. Div. 2008).***

A shopping center owner entered into a lease with a supermarket tenant. The lease did not impose an obligation on the tenant to reimburse the landlord for its legal fees and expenses if the landlord filed suit to enforce the terms of the lease after the tenant's default. The principals of the tenant signed a guaranty in which they agreed to pay the landlord, on demand, all costs and fees (including attorneys' fees) incurred by the landlord in enforcing the tenant's obligations under the lease or the principals' obligations under the guaranty. The tenant then assigned its interest in the lease to another supermarket operator, and the second tenant agreed to indemnify the original tenant against all claims or damages arising from its default under the lease. The second tenant then reassigned the lease to a third tenant, who agreed to indemnify both the original tenant and the second tenant from any and all claims arising from its failure to perform under the lease. The third tenant defaulted, and the landlord filed suit against the guarantors and the second tenant. The landlord estimated its lease damages at about $617,000, and its projected attorney's fees at about $32,000. The guarantors settled with the landlord for $30,000. The landlord then advised the second tenant that it was no longer pursuing a claim for attorneys' fees. Thereafter, the second tenant settled with the landlord for the sum of $500,000.

The guarantors sought to recoup the $30,000 under the theory of equitable subrogation. Under that theory, a party may be substituted in the place of another with reference to a claim, demand or right. Subrogation rights are created by agreement, by statute or by a court in order to "compel the ultimate discharge of an obligation by the one who should in good conscience pay it." The guarantors argued that the second tenant succeeded to the rights and obligations of the original tenant. They also argued that since they paid a debt of the original tenant, the guarantors should be obligated to reimburse them for that expense. On a motion for summary judgement, the lower court agreed. The second tenant appealed, and the Appellate Division reversed, noting that there was no contractual relationship between the guarantors and the second tenant, and there was no statute that would have compelled the second tenant to step into the guarantors' shoes under the guaranty. Rather, the only means to require the second tenant to reimburse the guarantors would be under the theory of equitable subrogation.

Here, the Court found that it was not equitable to require the second tenant to reimburse the guarantors, since there was no evidence that it knew of the guaranty when it agreed to assume the original tenant's obligations under the lease. The assignment of lease only required the second tenant to indemnify the original tenant for damages caused by a default under the lease but did not contain a provision requiring it to indemnify the guarantors for payments made under the guaranty. The Court noted that the guarantors could have negotiated an indemnification provision that would have obligated the second tenant to reimburse it for costs incurred under the guaranty but did not. The Court found that under those circumstances, it would be fundamentally unfair to require the second tenant to reimburse the guarantors. Second, the Court found that the doctrine of equitable subrogation is to be imposed against the one who should "in good conscience pay it." In this case, the Court noted that the third tenant was the primary defaulting party, and therefore it, and not the second tenant, was the party that should have paid. The reason the guarantors were seeking reimbursement from the second tenant was because the third tenant was not a financially viable entity. According to the Court, however, that was no reason to impose an equitable obligation on the second tenant.

Comment 1: The court characterizes the second tenant as an indemnitor, this doesn't strike the editor as quite accurate. An indemnitor is not primarily liable to the obligee, but only to another obligor (the first tenant). That wasn't the case here.

When the second tenant took the assignment of the lease, it assumed the lease. Hence, when the rent didn't get paid (albeit by the third tenant), the second tenant was liable directly to the landlord for the rent, at least under the general common law. Thus, in the editor's view, it was a surety for the performance of the debt. The landlord could have sued the second tenant directly, just as it could the first tenant. Indeed, landlord sued both first and second tenant directly, as the defaulting party, the third tenant, appears to have been broke.

The lease that second tenant assumed did not include an attorney's fee obligation. Thus, second tenant was not liable as a surety for the attorney's fees.

At the time of assignment and assumption, the second tenant executed a document that was characterized as an indemnification. This may have been superflous, in light of the suretyship rights of the first tenant. Perhaps the court viewed this as altering the nature of the second tenant's ordinary suretyship obligations, although it doesn't say so. In an event, the indemnification ran only to the first tenant, and not to guarantors. The indemnification did mention indemnification of obligations for attorney's fees, and of course there was no such obligation on the part of the first tenant, the court apparently views this "attorney's fee" language as meaningless surplusage.

At the time of the indemnification, the second tenant knew nothing of the guarantee of the first tenant's obligations nor of the attorney's fee obligation described there. The court made much of this. But, as described in Comment 2, however, the editor isn't sure this mattered at all.

Comment 2: What if the second tenant had known about the guaranty? Would that have changed things? In the editor's view, this wouldn't have changed the equities of the situation. The guarantors had an independent direct obligation to compensate the landlord for attorney's fees resulting from a claimed breach. To that extent, they were not guaranteeing the obligation of the first tenant, as the first tenant had no such obligation. Thus, the second tenant had no liability for those fees. They weren't the obligations of the first tenant. To the editor, it's as simple as that.

LANDLORD/TENANT; INSURANCE; TERRORISM INSURANCE: 1989 ground lease requiring standard extended coverage insurance does not allow ground tenant obtaining renewal policy in 2003 to purchase coverage that excludes the risk of terrorism. 1989 ground lease requiring standard extended coverage insurance does not allow ground tenant obtaining renewal policy in 2003 to purchase coverage that excludes the risk of terrorism**.** ***TAG 380 v. ComMet 380, 890 N.E.2d 195 (New York 2008***), discussed under the heading: "Insurance; Terrorism Insurance."

LANDLORD AND TENANT; LANDLORD LIABILITY FOR INJURY TO TENANTS; LEAD PAINT: Landlord was not entitled to summary judgment in tenant's action alleging lead paint injuries even where tenant did not specify either injuries or causation. ***Patterson v. Ahmed, 893 N.E.2d 198 (Ohio App. 6 Dist. 2008).***

In 1996, Appellants moved into a rental home at Toledo, Ohio where they remained until 2000. The home was owned by Appellee, Ahmed. Shortly after occupying Ahmed's property, Shaniece, then four, and Tiarra, then five months old, registered high levels of lead in routine blood screens. According to Appellants, Tiarra's lead level of eleven micrograms per deciliter ("ug/dl") on December 16, 1996, and Shaniece's level of twelve ug/dl on July 11, 1996 were sufficient to be classified as lead poisoning under standards promulgated by the Centers for Disease Control.

Appellants believed that the source of the lead in the children's bodies was paint chips from the windows in the ninety-year-old Hillwood house. According to an affidavit filed by Patterson, when she discovered peeling and chipping paint in the house, she requested Ahmed to remove or repaint the deteriorating surfaces. Patterson claimed that Ahmed promised remediation, but delayed action until pressured by the city housing authority.

In 2006, Appellants sued Ahmed, alleging that he knew or should have known of the presence of lead paint in the Hillwood house and that children susceptible to harm by lead paint would be occupying the structure. Appellants asserted that Ahmed's failure to abate the dangerous condition breached numerous common-law and statutory duties to appellants, resulting in injury to the minor children.

In his answer, Ahmed denied liability on the grounds that plaintiffs could not show that he knew of or indeed whether there was any such paint. Plaintiffs responded that Ahmed was an experienced real estate agent and landlord, and certainly knew that older houses in the Midwest commonly had lead paint.

Following initial discovery, Ahmed successfully moved for summary judgment. The trial court declined to rule on the grounds proposed by Ahmed, but held that Plaintiffs had not shown causation or actual injury.

On appeal: *Held: Reversed.* In his motion for summary judgment, Ahmed declined to address issues of proximate cause and damages and accepted appellants' assertion that the injury occurred. Because a passing allusion to a contested element is not sufficient to delineate it with specificity, the trial court's grant of summary judgment was improper. The Ohio District Court of Appeal thus reversed the trial court's grant of summary judgment and remanded the matter to the trial court for further proceedings.

LANDLORD/TENANT; MISREPRESENTATION; DISCLAIMER: Even where trial court finds that landlord willfully made or endorsed fraudulent representations to tenant in connection with commercial lease negotiations, such representations will not be actionable where lease contains a statement that tenant has not relied upon any statements by Landlord or its agents and a clause stating that the written lease is the entire agreement of the parties. ***Prudential Ins. Co. of America v. Italian Cowboy Partners, Ltd., 2008 WL 2841848 (Tex.App.7/24/08)*** (also discussed under the heading: "Landlord/Tenant; Rescission; Ratification."

Tenant was a successful and experienced restraunteur looking for a new location. It commenced negotiations with landlord to acquire a site in landlord's development. The negotiations continued for five months, and both sides were represented by counsel, Tenant's principles visited the site frequently.

After the lease was executed and tenant improvements commenced, the tenant's employees noticed an occasional sewage smell. Tenant complained to Landlord, but completed the tenant improvements and opened for business. Landlord commenced efforts to resolve the intermittent sewage smell problem. Later, a guest at the restaurant informed Tenant that the prior restaurant located at that location had experienced the same problem and had never been able to correct it.

After further efforts to resolve the problem were unsuccessful, and after Landlord informed the Tenant that Tenant would be responsible for any further remediation, Tenant closed the restaurant, stopped paying rent, and sued for fraud, negligent misrepresentation, breach of quiet enjoyment, and constructive eviction. Landlord counterclaimed for damages. The trial court found for Tenant and awarded damages in excess of $1 million, exemplary damages, and attorney's fees.

On appeal: *Held: Reversed.*

This is a very rich case, with many issues of particular benefit to landlords, especially those in Texas. We'll focus on several of them here. It should be noted, however, that, based on the litigation history of the parties, we may see a further appeal here. Thus far Westlaw doesn't show any action on appeal.

The first issue addresses on appeal was whether Tenant was barred from raising claims of fraud and negligent misrepresentation by disclaimers contained in the lease.

The trial court had found that the Landlord's agent, in representations endorsed by Landlord, had stated during negotiations:

a. The premises (although known to have been occupied by a prior restaurant) "was practically new and was problem-free."

b. No problems had been experienced with the Premises by the prior tenant;

c. The building on the premises was a perfect restaurant site [and a bargain].

Although these might be construed as statements of opinion or "puffery," the trial court concluded that they were intended as statements of fact based upon the agent's experience in the industry and with the building.

The Court of Appeals assumed these findings were binding, but concluded that they meant nothing because the Tenant, in the lease, had agreed that Landlord and its agents had not "made any representations or promises with respect to the Site, the Shopping Center or the Lease except as expressly set forth [in the lease]." The lease further contained an integration clause stating that this was the entire agreement of the parties.

Although the Court of Appeals acknowledged that a 1997 Texas Supreme Court case had found that prior authority in Texas was not "entirely consistent" on the question of disclaimer and merger clauses. That case, however, had tried to establish a clearer precedent going forward. But the case acknowledged that there are circumstances in which it would be inappropriate to give credit to a disclaimer, where the circumstances of the agreement suggested a lack of full understanding of the provision or otherwise indicated that the agreement was not fairly reached between thoughtful and knowledgeable parties. But here, the opposite was true. The parties knew what they were doing, and should be held to their agreement:

"Not every disclaimer of reliance or merger clause will bar a fraudulent inducement claim . . . However, when we review this record and consider the circumstances surrounding the formation of the lease, we find that the parties were represented by counsel as well as real estate brokers both before and during the negotiations leading up to the singing of the lease and guaranty. The record also reveals that the parties to this arm's length transaction were sophisticated in dealings involving the leasing and the operation of restaurant properties, that several drafts of the lease were circulated and that various changes were negotiated and made to both the lease and guarantee."

Thus, the disclaimer was upheld.

Comment: Note that the argument here was "fraudulent inducement." Such a claim has been held to survive "as is" clauses and similar waivers of claims in other jurisdictions. But many of those cases did not involve the balanced bargaining environment that we have here. This case is certainly a major benefit to sophisticated parties who wish to be able to rely on their agreements. It may also be a caution to sophisticated parties who are asked to enter into such agreements. They may want to restrict the scope of a disclaimer to take into account deliberate fraud.

As a practice guide, it would appear wise for practitioners to keep records of the bargaining history of a given deal and to make sure that there in fact is open and fair bargaining. The editor has heard recently that some litigators are telling their transactional colleagues to dump all records of bargaining after a deal is done. This is inconsistent with the way that the editor learned to practice, and he remains uncomfortable with the idea for a number of reasons. This case adds one more.

Also see ***Daines v. Vincent, 2008 UT 51, 190 P. 3d 169 (Ut. 2008)***, discussed under the heading: "Contracts; Integration Clause." The *Daines* case also involved a fraud allegation that the court concluded had been waived in a separate agreement. The court held that an integration clause in a waiver of claims that clearly states that the contract supercedes any other agreements dispels any possible ambiguity as to whether all prior claims are waived, as opposed to those that gave rise to the settlement involving the waiver.

LANDLORD/TENANT; RENT; RENEWAL RENT; APPRAISAL: When valuing a premises for the purpose of determining rent for a renewal term, the value of the net lease should be taken into consideration. ***936 Second Ave. v. Second Corporate Dev., 861 N.Y.S.2d 256 (Ct App. 2008).***

Tenant had a 20-year commercial net lease that included the option to renew lease for two additional 20-year periods. In the event of renewal, the annual rent would be seven percent of the value of the demised premises as of the date of the commencement of the successive period.

The lease defined the value of the "demised premises" to include the value of both the land and buildings and improvements located upon it, but was silent as to whether the lease itself should be taken into account when determining the value.

In court, tenant argued that though the lease may impact the value of the property, the absence of any language expressly requiring the consideration of the lease itself means that the appraisers were obligated to ignore it when forming their valuations. Landlord countered that because the net lease affected the property value, it must be considered unless the lease specifically precluded the appraisers from taking it into account.

The Court cited case law that stated when valuing real property, "[s]pecial attention must be given to limitations on ownership rights, which include easements, encroachments, leases, and the disposition of air or subsurface rights," and even though appraisers generally consider the highest and best use of the property in determining its value, in order to do so they necessarily must examine any restrictions or limitations, including long-term leases, that may impact the highest and best use for which the property may be utilized. Therefore, the court concluded that the net lease must be taken into account here, and if the parties to a lease do not wish the lease to be taken into account all they need to do is to include language to that effect in their lease.

Comment: Looked at mechanically, of course the present value of the property must take into effect all factors, including contractual encumbrances, that enhance or reduce it's appeal to the market. And the existence of the lease does have an impact. In this case, it appears, the existence of a creditworthy tenant that apparently intends to remain increased the value of the property in the marketplace. Of course, it is just as possible that an existing lease might be below market or belong to an undesirable tenant and would reduce the market valuation of the property. In such case, one assumes, both landlord and tenant would take exactly opposite views of the situation from those they took here, and again argue that their respective views are supported by unassailable logic.

Comment 2: But it is appropriate to take a mechanistic view here? Is the notion that the lease is part of the value really consistent with the probable intent of the parties? Remember that, at the outset, 20 years before, either landlord or tenant could have been burned by this interpretation. It doesn't strike the editor as logical that either side would have expected that a "fair value" clause would be impacted by whether or not the tenant was a creditworthy tenant in the market view. Further, there is something circular in computing the rent based upon market value, including the existence of a lease, when the rent under that lease has an impact in market value itself.

Cases cited by the court in which there were third party-owned encumbrances that had an impact on value are, of course, inapposite. But the court did have a New York precedent in which the parties had agreed that the property was to be valued as if it were vacant in determining renewal rent, and the court proceeded to include the existing lease as relevant to that value. Both that case and this one, incidentally, involved triple net leases.

All of the editor's judgments in writing these comments are, of course, "saddleback shots," taken with relatively short reflection. But the editor feels that in both the precedent case and this one, the original parties, at the time of the original bargain, expected the land to be valued without taking into account the impact of the lease that was the very subject of the rent negotiation.

LANDLORD/TENANT; RENT; RENEWAL RENT: Renewal rent "cap" based upon rent paid by an identified other tenant "or successor" will not be used when the identified tenant has gone out of business and the rented space has been subdivided and leased to a variety of tenants. ***California Nat'l Bank v. Woodbridge Plaza, LLC 164 CA4th 137, 78 CR3d 561 (2008).***

Tenant's existing 25-year lease included an option to extend for an additional 10 years, at a rent that equaled "the then prevailing rate," but one that would "not exceed the latest square foot rental paid by the Bank of Irvine or successor in Woodbridge Plaza for ground floor space."

The Bank of Irvine had long since gone defunct and no longer occupied space in Woodbridge Plaza. By the time that Tenant's original lease term expired, the Bank of Irvine's space had been subdivided and was now occupied by professional offices. Tenant argued that the present tenants of that space were "successors, and that the rent cap provision applied, leading to a relatively low $1.50 per square foot – the "blended rate" for those tenants, ranging from medical offices to a hair salon.

The court rejected this argument and also tenant's claim as to prevailing market rate (which was based upon a study that excluded financial institutions), and set the rent at $3.00 per square foot. It derived this from landlord's appraiser, who drew upon market date for similar depositor financial institutions in the area.

The court basically held that the "cap" in the lease had no meaning, as it didn't refer to the space, but to successors of the Bank of Irvine, and there were none.

Roger Bernhardt's Comment 1: The result is one that I think most observers would also reach, since the remaining provisions of the lease and the business purposes of the parties all appear to point in that direction.

Daniel Bogart's Comment 1: Yes, most laymen and even many lawyers would assume that the lease contract's reference to "successor" would be limited to a successor in the same business (banking). Roger is right that this was probably the intention of the parties. The economics of the lease transaction suggest that the parties wanted a "comparable" tenant to use for rent comparisons: Thus, the Bank of Irvine was used and not a doctor's office.

Still, it is not clear to me that the court was right in validating this assumption. The contract, at least as repeated in the opinion, caps rent at the rate of Bank of Irvine or its "successor." Arguably, the rental provision melds into the use of the property. If we digress to use clauses generally, we find that parties to a lease must employ explicit language to restrict uses of property. (For example, if the original S&L lease stated that the premises "shall be used for a banking facility," most courts would view this as permissive language only. Barring other language limiting assignment, the tenant could assign its lease to a massage parlor if it so chose.) Now, look at the scenario in Woodbridge Plaza. All this lease says is that the rent will be capped at the rate paid by the Bank of Irvine or its successor. There is nothing on the face of the lease to indicate that the actual business use of the successor matters; the word "successor," taken alone, is permissive.

To make this concrete, assume a change in facts. What if, instead of going belly up, Bank of Irvine had assigned its lease, with the landlord's permission, to an upscale accounting firm, which then occupied the entire premises? The assignment would be for the full duration of the term of the lease. We might even assume, for good measure, that the accounting firm signs an assignment and assumption agreement. I doubt seriously that this court (or any court) would have denied that the accounting firm was a "successor" to Bank of Irvine. Could the landlord really walk away from the rental cap because the "business" of the successor differed from the original Bank of Irvine?

In fact, the *Woodbridge Plaza* facts involved a triple net lease. There were no percentage rents, and the landlord did not have to cover other large expenses sometimes associated with leasing commercial space. This limits the importance of finding a comparable business on which to base the rental cap. The only real comparable elements that should matter are that a single successor takes the whole space, subject to a triple net lease. In Woodbridge Plaza, the alleged "successor" was a group of tenants with an averaged rental rate. Perhaps this would have been a better basis on which to say the new tenants were not the "successor" to Bank of Irvine.

The comments above are from the California CEB Real Property Reporter, contributed by Roger Bernhardt at Golden Gate Law School (well known to DIRTers) and Daniel Bogart, a professor at Chapman Law School and the co-author of law school teaching materials on commercial leases. The original report came from the same source, but the editor has changed it substantially.

LANDLORD/TENANT; RESCISSION; RATIFICATION: Tenant's act of insisting that lessor make certain repairs – which repairs tenant understood to be lessor's obligation under lease – ratified the lease, such that lessee could not avoid lease on basis of mistake, even where the repairs in fact were not required by law. ***Prudential Ins. Co. of America v. Italian Cowboy Partners, Ltd., 2008 WL 2841848 (Tex.App.7/24/08).***

The basic facts of this case are reported under the heading: "Landlord/Tenant; Misrepresentation; Disclaimer."

It is difficult to know exactly why the appeals court took up the issue of Tenant's argument that it had a right to rescind the lease on the basis of mutual mistake. Of course, since the lower court had found constructive eviction, Tenant didn't need to rescind. Perhaps, on remand in order to address the landlord's damages claim, the appeals court found it helpful to deal in advance with Tenant's rescission claim.

The court tells us almost nothing specific about Tenant's claim except that it was based upon "unilateral or mutual mistake." One assumes that the claim was based upon the same operative facts as the principle dispute – information about the sewer smell. Here, apparently, Tenant is accepting the argument that there were no specific representations about sewer gas, but a general lack of information about the suitability of the premises for a restaurant. (The court points out, by the way, that a subsequent Tenant, paying for it's own repairs, fixed the sewer smell rather quickly.)

The court found that Tenant waived its claim when it pressed what it saw to be its rights under the lease and insisted that Landlord repair the sewer gas smell. In another part of the opinion, the court found that the likely source of the smell was not structural, and within that portion of the premises as to which Tenant assumed responsibility for repairs. Further, the court found that there was no "implied warranty of suitability" applicable here, as the allocation of repair responsibility to Tenant negated any implied warranty. So, even though Landlord in fact had no duty to fix the problem under the lease, Tenant's insistence that Landlord proceed to fix the problem, and Tenant's occupancy for a number of months beyond that point, indicated that Tenant had chosen to operate under the Lease and could not later say that the presence of the sewer gas justified rescission.

Comment: Although somewhat special facts, the editor suspects that this notion of ratification of the lease, even based upon a misapprehension of its terms, will prove valuable in litigation for some landlord's lawyer someplace, and might even prove useful to a tenant's lawyer.

Is it correct? Why not? Rescission is a pretty dramatic remedy, and where a party, instead of resorting to rescission, proceeds to continue with the lease and, in this case, receive landlord's efforts to cure the problem and further occupies the operates on the premises, the tenant creates a situation where rescission doesn't seem quite just.

LANDLORD/TENANT; TERMINATION OPTIONS; LATE NOTICE: Late notice of lease termination will not be excused because of sloppiness in providing notice to the property address. ***Genesco v. N. LaSalle Partners, 889 N.E. 2d 769 (Ill. App. 2008).***

LaSalle was a subtenant under a three and a half year sublease with Credit Suisse of certain retail space. At the time of entering into the sublease, LaSalle also entered into a six year lease (the "Future Lease") with Associates, the prime landlord of the building, that commenced following the termination of the Credit Suisse sublease, on February 28, 2008. Obviously, the lease term under the Future Lease with Associates began substantially later than the time of execution of the lease. LaSalle was apparently intending to "lock in" what it thought to be valuable space, and guessing that the rent would be at or below market when the lease took effect.

The Future Lease provided that LaSalle could terminate the lease before the term started by paying $30,000 termination fee and by giving written notice to "Landlord" on or prior to February 28, 2007. The notice was to include a $7500 "first installment" of the termination fee. Although the sublease defined Credit Suisse as "Landlord," and identified Associates as "Overlandlord," there was no such definition in the Future Lease (not surprising – since the only parties were Tenant LaSalle and Landlord Associates.) (Genesco later took over Associates' position here, but its presence is irrelevant to the analysis or outcome.) Time was stated to be of the essence.

As February, 2007, drew near, LaSalle apparently realized that the base rent of the Future Lease would be over market, and attempted to renegotiate the base rent, telling Associate's agent that if there could be no renegotiation, it would terminate. The negotiations were unsuccessful, and LaSalle's agent notified Associate's agent by telephone that LaSalle would exercise its termination option.

Here's where things got messed up: The Future Lease had a specific and detailed notice provision, that stated that notices were to be address to Landlord at the specified address of its agent, and that notice would be deemed given, whether or not received, on the date delivered by an overnight courier service or two days following the date when deposited in the United States Mail . . . "**properly addressed.**" (Oops).

On February 27, 2007, apparently looking at the sublease, LaSalle's agent sent mailed notice of termination, with the required check, to Credit Suisse, with copies of the notice to Associates. Of course, sending notice to Credit Suisse, which was merely the sublandlord, did not satisfy the notice provision. Further, the address it used for Associates was "suite 200," instead of the correct "Suite 2000" as set forth in the notice provision in the Future Lease. Associates' agent didn't get the copy of the notice. Note that, in any event, the mailing was too late to meet the notice requirement, even if it had been sent to the correct party and properly addressed.

On March 7, LaSalle's agent got the check back from Credit Suisse and attempted to set things right, but garbled things again and sent the check and notice to the wrong address, notwithstanding the fact that the notice address in the Future Lease hadn't changed. Ultimately, Associates returned the check.

There was no evidence that Landlord had changed its position in the few weeks it took to get the notice to the right party, and of course actual notice of intent to exercise the termination provision was provided prior to the expiration time by phone call. Nevertheless, the trial court awarded summary judgment to Associates (now Genesco) disallowing the untimely termination. The appeals court here affirmed.

The situation, as viewed by the court, is similar to that in the seminal 1900 case of *Dikeman v. Sunday Creek Coal Co."* That case admitted that there is a limited role for equity to set aside the result compelled by the legal analysis of the instruments – which result would be that tenant has no rights except through strict compliance with the lease. But *Dikeman* limited the role of equity to circumstances in which there was a strong equitable excuse for non compliance: "[Tenant} lost its legal right by failing to comply with the condition precedent, and we do not see how equity can relieve against mere forgetfulness."

A later case, *Thomson Learning, Inc.,* set a test that focussed more on the degree of hardship resulting from the tenant's loss if its expected right, rather than adequacy of the excuse:

"To be entitled to equitable relief, a lessee that fails to strictly comply with an option to cancel or extend a commercial lease must at a minimum establish: (1) the delay in strictly complying was slight; (2) the lessee would suffer undue hardship if strict compliance were not excused; and (3) the lessor would not suffer hardship if strict compliance were excused." (Citing Corbin)

Although the appeals court spent a great deal of space discussing whether the tenant's error here was "justly excused," and in fact argued that the *Thomson* case was incorrect in embracing the Corbin test it did go on to consider the factors emphasized in *Thomson* – whether undue injury would result.

Both the trial court and appeals court took into account the fact that the damages to LaSalle for being forced to carry out its six year lease were, in the view of the court, lower than the $1 million gross rents contended by LaSalle. LaSalle could sublet or assign and mitigate its loss. If LaSalle in fact did not pay the rent, it noted, the landlord certainly would mitigate its damages. The rest of the opinion more or less assumes that the injury to the tenant is irrelevant if the tenant misses the notice requirement, so it should be noted that the court did address this consideration even while denying the relevance of it. It concluded that the damages tenant would suffer would be no more than "ordinary business losses" from making a bad business decision.

A concurring opinion by Judge Theiss notes that the majority opinion is a bit schizophrenic in failing to choose between the focus on the degree of excuse and the hardship of the result as the primary consideration here. The concurrence notes that Williston on Contracts suggests a test that takes both the adequacy of the excuse and the degree of forfeiture into account. "Late exercise of an option may be excused where: (1) the failure is caused by inadvertance or oversight; (2) the other party has not substantially changed position in reliance on the failure; (3) the application of the general rule that time is of the esse3nce would work an unconscionable result or a forfeiture."

The concurrence characterized *Dikeman* as holding that only fraud, accident or non negligent mistake would justify setting aside the consequences of an untimely exercise of an option. It maintained that, in essence, this element of *Dikeman* has been overruled by subsequent cases granting relief in cases that fall short of that level of excuse. It maintains that appellate courts in Illinois have applied the Williston three part test set forth above.

The court further maintains that where the failure to exercise timely has resulted from factors completely outside the control of the exercising party, hardship need not be shown. Remember, this is the concurrence.

Comment 1: So we are left with a somewhat muddled analysis, but one that seems to conclude that both the degree of excuse and the degree of hardship will be relevant in Illinois, but that the "fair excuse" test will be somewhat strictly maintained, at least where extraordinary losses cannot be shown to result.

Comment 2: There are other jurisdictions that are more strict on option exercise, viewing it as a condition for a right, and concluding that there is no "good faith and fair dealing" requirement where the right simply was not brought into being by satisfaction of the conditions in the contract. But we have cases finding otherwise. Perhaps the most colorful was Brunswick Hills Racquet Club, Inc. v. Route 18 Shopping Center Assoc., 2005 N.J. Lexis 7 (1/ 25/05) (the DIRT DD for 2/4/05), where the Supreme Court of New Jersey discussed good faith and fair dealing principles in finding that tenant's failure to provide a proper formal exercise of an option to purchase was excused where landlord stalled and mislead tenant until after option deadline had passed without telling tenant that it expected a lump sum price for lease renewal simultaneous with notice of exercise of tenant's option. Tenant had provided the necessary notice, but had anticipated paying the option price at a later closing. [Note that the potential forfeiture in *Brunswick* was much greater than in the instant case.]

MECHANIC'S LIENS; LIENABLE WORK; CLEANING OUT CORPSE: Does removal and disposal of bodily fluids that seeped from a decomposing dead body into carpet, sub-flooring and basement, and which were absorbed throughout the house constitute labor for the "repair" of the house within the meaning of mechanic's lien statute? ***Midwest Biohazard Services, LLC v. Rodgers, Indiana Court of Appeals, Case No. 41A05-0805-CV-290, 2008 Ind. App. LEXIS 2038 (Ind. Ct. App. 2008).***

Midwest Biohazard Services ("Biohazard") appealed from the trial court's dismissal of its claim to foreclose on a mechanic's lien. The trial court had dismissed Biohazard's complaint for failure to state a claim upon which relief could be granted, concluding that Biohazard's services were merely cleaning and, as such, were not labor or materials for the "repairing" of the house within the meaning of the Indiana mechanic's lien statute.

On October 5, 2001, Mr. Rodgers conveyed his residence in Johnson County, Indiana, to The Hugh C. Rodgers Trust (the "Trust") but remained living there. In 2007, he died while home alone [apparently, although we are free to speculate wildly as to cause of death, which is not mentioned in the opinion] and his body, undiscovered and decomposing where it lay for several days, leaked fluids that seeped into and through the carpet and sub-flooring, then down into the basement. The decomposition of the body also caused the absorption of contaminants throughout the house. After discovery of the body, Rodger's son contacted Biohazard, obtained an estimate of $13,500 for the cost to remove and dispose of biohazard waste caused by the decomposition of the senior Mr. Rodger's body. Biohazard and the son then executed a contract, and the son paid $1,150 as a deposit for Biohazard's services. A few days later, Biohazard began the work, but after several days of performing decontamination services, the son made Biohazard aware that he did not intend to pay for Biohazard's work. [Interestingly, the opinion does not say why the son refused to pay, nor does it say whether Biohazard finished the work.] Shortly thereafter, Biohazard filed a notice of its intention to hold a mechanic's lien with the Recorder of Johnson County.

In December, 2007, Biohazard filed its complaint against the son, as well as against the Trust to foreclose on the mechanic's lien, attaching a copy of the work description in the estimate that formed the basis for the services contract, which included "removal of carpet and pad in the hallway, living room, and dining room; cleaning and disinfecting the ceiling, walls, and floors throughout home; and cleaning and disinfecting the concrete floor in basement." The Trust and the son filed a motion to dismiss the portion of Biohazard's complaint seeking foreclosure pursuant to Indiana Trial Rule 12(B)(6) (failure to state a claim upon which relief can be granted), and their motion was granted.

On appeal, Biohazard contended that the services it had allegedly provided in removing and disposing of the contaminants were "repairs" that fall within the scope of the Indiana mechanic's lien statute. The Trust and son responded that the services allegedly performed by Biohazard were merely cleaning services, which fall outside the scope of the statute.

The Indiana mechanic's lien statute confers upon contractors and other persons the right to file a mechanic's lien for, in relevant part, "performing labor or furnishing materials" for the "erection, altering, repairing or removing" of a house or other building or structure. Ind. Code §32-28-3-1. The court first stated that because the mechanic's lien statute derogates common law, Indiana courts have strictly construed it in determining its scope, including when a person is entitled to acquire and enforce a mechanic's liens. Therefore, the claimant has the burden to prove that his or her claim is within the scope of the statute. Once the claimant has met this burden, however, the statute is liberally construed to accomplish the statute's remedial purpose. Quoting from a 1913 Indiana Supreme Court opinion, the court pointed out that the "underlying motive" of mechanic's lien laws is "justice and equity in dedicating, primarily, buildings and the land on which they are erected to the payment of the labor and materials incorporated, and which have given to them an increased value" and that "[t]he purpose [of mechanic's lien laws] is to promote justice and honesty, and to prevent the inequity of an owner enjoying the fruits of the labor and materials furnished by others, without recompense."

Given that there is no dispute as to whether Biohazard was a contractor or person "performing labor" as contemplated by the statute, the court noted that the only dispute was whether Biohazard performed tasks that would qualify it for protection under the mechanic's lien statute. The trial court had concluded that Biohazard's services were mere "cleaning" services, and not covered by the statute. "Repairs," however, are covered.

"Repair" is not defined in the statute, so the court cited the rule of construction that "undefined words in a statute are given their plain, ordinary, and usual meaning," as may be found in English language dictionaries. Looking to Webster's Third New International Dictionary (2002), the court first noted that the commonly used definition of "repair" as "to restore by replacing a part or putting together what is torn or broken" would not fit Biohazard's alleged services. However, "repair" also is defined as "to restore to a sound healthy state," which, the court concludes, clearly includes the decontamination of the house performed by Biohazard. Seeing no reason why the mechanic's lien statute's use of the word "repair" should not include the dictionary's second "plain, ordinary, and usual meaning" of restoring property "to a sound healthy state," as well as the more common definition of restoring it by "replacing a part or putting together what is torn or broken," the court concludes that Biohazard's alleged house restoration services required in the wake [pun intended] of Mr. Rodger's undiscovered decomposed body are literally comprehended by the mechanic's lien statute.

Turning to policy grounds, the court reprised the 1913 Indiana Supreme Court opinion to the effect that the purpose of the mechanic's lien statute "focuses largely on whether the activities performed upon the property increased the value of that property." "It takes no stretch of the imagination, " said the court, "to recognize that a buyer would be willing to pay more for a house that was free from biohazard contaminants than she would be willing to pay for the same house in a contaminated state." Thus, the services allegedly performed undoubtedly increased the value of the house. In conclusion, the court reversed the trial court, holding that Biohazard has stated a claim upon which relief can be granted and the motion to dismiss was improvidently granted.

Reporter's Comment 1: It is unclear whether the opinion might be extended to cover "ghostbusting" and exorcism or other such services to eliminate spirits, ghosts, goblins or other unwanted entities from houses and other structures (elimination from persons presumably would not qualify, unless the person is so attached to the structure as to constitute a fixture). There is legal precedent that the presence (or reputed presence) of such entities may adversely affect value. *Stambovsky v. Ackley,* 169 A.D.2d 254, 572 N.Y.S.2d 672 (NY Sup.Ct. 1991) (Noting that if *caveat emptor* applied, the buyer didn't have "a ghost of a chance" of winning, the court observed that even the "most meticulous inspection and search would not reveal the presence of poltergeists in the premises or unearth the property's ghoulish reputation in the community." Because the seller previously had encouraged publicity fostering the belief that the house was haunted and took advantage of the out- of-town buyer's ignorance by failing to inform him of the house's reputation, which the court considered an adverse condition not discoverable by a reasonable inspection, the court granted rescission. Buyer got his money back and seller got the ghost. No, I did not make this up.)

Reporter's Comment 2: The court seems to accept the view that mere cleaning, as such, does not constitute an alteration or repair of property under the mechanic's lien statute, although "restoring to a sound healthy state" could certainly encompass cleaning services of a lesser nature than biohazard contamination removal. And, as to the issue of enhancing value, any broker will attest that an unclean house or building will fetch a lower price than one that is clean.

There seems to be a dearth of Indiana law on the "clean" vs. "repair" distinction, but a quick search turned up cases in Ohio and Pennsylvania where courts have held that their mechanic's lien statutes do not cover cleaning services. *Midland-East Sales Corp v. Adams Sewer, Inc., 1985 Ohio App. LEXIS 7329* (dredging and removing debris from storm sewers do not fall within plain and ordinary meaning or "alter" or "repair" in mechanic's lien statute); *King's Oak Liquidators v. Bala Cynwyd Hotel Associates, 405 Pa. Super. 250*; *592 A.2d 102 (*cleaning, verifying inventory, securing buildings, cleaning supplies, security services, including the cost of chains and locks, do not qualify under Pennsylvania mechanic's lien statute: "security services performed during construction of a building are not protected by the Mechanics' Lien Law. *Metropolitan International v. Union Investment Co., 17 Pa.D. & C.3d 519 (Phila. 1981).* It has also been held that the removal of trash as part of a contract to demolish a building is not protected. *Jan-Lee Corp. v. Thompson Realty Co., 3 Pa. D. & C.2d 457 (Phila. 1954)*"). Of course mechanic's lien statutes in some other states that did not turn up may be more liberally worded or construed.

Editor's Comment 1: For a related case, see *Kennedy v. Kidd,* 557 P. 2d 467 (Okla. App. 1976), where the court found that a deceased tenant's estate was not liable to the landlord for similarly grim clean up costs when the tenant died alone in the apartment and was not discovered for a week. (In the summer, in Oklahoma). Although a tenant owes a landlord the duty to return the premises in a reasonable condition upon lease termination, this liability does not extend to the tenant's estate when the tenant dies on the premises. (???)

Also see: *Yates v. Kaplan,* 347 N.Y.S.2d 543 (N.Y. Misc. 1993) (Where statutory tenant dies in apartment, companion/caretaker residing with him, who moves out during clean up, cannot be locked out thereafter without summary possession action, even though she has no further rights of possession.) This case needs to be read as one of the great epics of judicial literature – written by extremely colorful law professor, judge and former thespian, Irving Younger.

The Reporter for this item was Rory O'Bryan of the Indianapolis Bar.

MORTGAGES; CHARACTERIZATION; EQUITABLE MORTGAGES: Sale/leaseback involving distressed homeowner may be recharacterized as an equitable mortgage notwithstanding extensive language in the documentation of the transfer denying that a mortgage relationship exists. ***Bernstein v. New Beginnings Trustee, LLC, 988 So. 2d 90 (Fla. App. 2008).***

Bernsteins, who alleged that they had fallen behind in their mortgage payments due to illness, were facing foreclosure of their property. The accelerated claim of the mortgagee was $88,000, but under the terms of their mortgage, the Bernsteins retained a right to cure and reinstate the mortgage for $32,000. They alleged that their property was worth $250,000 at this time.

A few weeks before the foreclosure sale, Bernsteins were approached by New Beginnings New Beginnings, which offered to buy the property by paying the reinstatement monies, $32,000 to the lender, and to give Bernsteins a one year lease with option to repurchase their home for $125,000. During the terms of the lease, Bernsteins alleged, New Beginnings was to pay the mortgage payments.

The documentation of the transaction acknowledged that the sale price might not reflect the market value of the property, because it was a "distress sale." The documentation also stated that the Bernsteins were not acting under duress and was at "arms length." Indeed, the Bernsteins, at the trial court, acknowledged that they had full knowledge of their actions and had the advice of legal counsel. (They alleged, however, that the lawyer given to them was counsel to New Beginnings.)

The lease provided that the rental payments would be used to pay the existing mortgage on bgehalf of the Bernsteins and that any additional funds "will be deemed to cover administrative and overhead costs and time and efforts expended [by New Beginnings.]" Under the lease, the Bernsteins undertook all responsibility for maintaining and repairing the property, even, specifically, structural repairs. Bernsteins were responsible for special assessments, insurance and tax increases (presumably the base property taxes were covered in the mortgage payments) and the condo association fees. (Note that the agreement to maintain and repair likely was inconsistent with New Beginnings responsibility under the implied warranty of habitability, assuming Florida, like most states, would apply that doctrine to townhomes.) There is no indication from the court report that New Beginnings even recorded the deed, or that it notified the lender of the transfer. (Likely, of course, the transfer would have given the right to the lender to accelerate again under the due on sale clause.)

The court concluded that "all indicia of ownership" remained with the Bernsteins, and that Bernsteins didn't even give New Beginnings a set of keys. Notwithstanding all of this, when the Bernsteins later failed to pay rent, alleging that New Beginnings was not maintaining payments on the mortgage, the trial court rendered partial summary judgment for New Beginnings, finding that the sale and leaseback were valid and granting New Beginnings a writ of possession of the property.

The appeals court reversed and remanded for further proceedings, finding that this transaction was in fact an equitable mortgage, and that therefore Bernsteins' interest could be terminated only through a foreclosure action. It found it unnecessary to reach at this point the intriguing other issues raised by Bernsteins – that this was a residential mortgage as to which TILA applied, justifying rescission of the transaction by the borrowers and damages (and, presumably, attorney's fees) as none of the federally required disclosures were made.

Comment 1: The only remarkable aspect of this case was that the trial court judge didn't recognize an equitable mortgage arrangement when it stood up and crowed like a rooster. Classically, self serving language in the instruments of these disguised mortgages does not avail the "lender." What is far more significant is the fact that the borrower has sold the property for substantially less than its value and also has a right to reaquire the property for substantially less as well, indicating an "economic compulsion." Here, the $125,000 option price was much lower than the alleged $250,000 value of the townhome, but also gave the lender a return of around 300% on the $32,000 it "loaned" to the Bernsteins at the outset.

Of course, since the original determination by the trial judge was summary judgment, we haven't yet had a trial of the facts, and it may be that Bernsteins won't be able to prove the values that they allege. Nevertheless, the fact that this deal was made under economic stress and that New Beginnings did not in any way accept the responsibilities of being a landlord are likely to carry the day in establishing finally that we had a mortgage here.

Comment 2: Although the outcome is unremarkable, the setting of the case as part of one of the many spurious "home foreclosure" rescue schemes now being perpetrated on homeowners during the current crisis makes the case noteworthy.

Comment 3: Note that in a commercial sale/leaseback transaction, it would not be uncommon for the transferor to retain possession and undertake all "indicia" of ownership, executing a triple net lease imposing all responsibilities on the tenant. In such a case, the court would likely look much more carefully at the economics of the transaction – the sale price and the option price, to determine whether it ought to recharacterize a deal as a mortgage. In fact, in the area of synthetic leases, recharacterization is so common that the parties in fact rely upon it and get title insurance to protect the alleged "buyer/landlord's" status as an equitable lender, which is a status it would prefer in the event of the "seller/tenant's" bankruptcy.

MORTGAGES; DISCHARGE; SATISFACTION STATUTE: Ohio Court approves class certification in action for violation of mortgage satisfaction statute. ***Radath v. Federal National Mortgage Association, 891 N.E.2d, (Ohio App.6th Dist. 2008).***

Radath entered into a loan agreement on December 6, 2000, regarding real property in Cleveland, Ohio. The mortgage was recorded on December 11, 2000. Radath paid the mortgage in full on or about August 28, 2002, and the entry of satisfaction was filed on November 29, 2002. Ohio Revised Code Section 5301.36 requires filing of satisfaction within 90 days. For any one violation, the statutory penalty is $250.

On August 7, 2003, Radath filed a class-action complaint against FNMA alleging violation of the statute. Radath's proposed class consisted of: "All persons who, since May 9, 1997 and thereafter, paid off residential mortgages recorded in Ohio, where FNMA was the mortgagee at the time of mortgage satisfaction and where the mortgage satisfaction was not recorded within 90 days." The trial court granted Radath's motion for class certification and denied Radath's partial motion for summary judgment.

FNMA appealed asserting three assignments of error: superiority, identifiability, and predominance. FNMA argued that the element of superiority was not satisfied because the trial court failed to recognize the existence of parallel class actions against mortgage servicers that covered half of the putative FNMA class members. FNMA argued that because it hired servicers to manage the mortgages and to file entries of satisfaction, it was not the proper defendant in this case. FNMA argued that a superior method for fair and efficient adjudication required that the proposed class members recover against mortgage servicers.

The Appellate court found that the interest of members of the class in individually controlling the prosecution of separate actions is low because the recovery for each mortgagor was only $250. The Court further found that a high desirability to concentrate litigation of the claims in a particular forum exists. In granting class certification in the instant case, the lower court avoids duplication of time, effort, and resources because FNMA acted as mortgagee to 981,861 mortgages that were satisfied during the time frame set forth by the class-certification order. The Court, therefore, overruled FNMA's first assignment of error.

In the second assignment of error, FNMA argued that the certification order failed to identify any objective means for ascertaining membership in the class. The Court found that there is no law requiring that the class members in this action be ascertained from public records, nor is there a law requiring that the class-certification order identify the exact means by which class membership will be ascertained. Therefore, the Court overruled FNMA's second assignment of error. Finally, FNMA argued in its third assignment of error that common issues did not predominate over individualized issues. The key issue regarding this assignment is whether FNMA violated R.C. 5301.36 by failing to timely record a satisfaction of mortgage. The Court noted that the trial court is in the best position to consider the feasibility of gathering and analyzing class-wide evidence. Because the trial court's ruling did not exceed the bounds of reasonableness, the Court found that it acted within its discretion in resolving that there were common questions of fact among class members that could be presented in an efficient manner.

As to the argument that the servicers were in fact responsible, Ohio Revised Code Section 5301.36 makes no provision for mortgage servicers. Therefore, courts have not found issue with class-action lawsuits against the mortgagee where servicers were responsible for recording the satisfaction. Thus the trial court did not err in finding the element of predominance satisfied and FNMA's third assignment of error was overruled.

Comment 1: Late mortgage satisfactions were a serious problem in the late lamented "hot market." Many states enacted statutes with relatively severe penalties for foot dragging in this area. Another example of how chaotic things had become is that, despite this fact, servicers nevertheless messed up the timing of releases. To the editor, there's really no excuse for being unable to grant a release within 90 days of payoff. If things are so confused that a servicer can't get that done, then it's time to unconfused.

Although FNMA looks like it will get tagged with a big judgment here, it likely will be able to lay liability off in its servicers, if they're still in business. In any event, we really aren't that sure just how many mortgagees got late releases. The class action lawyers may not enjoy the payday they anticipated (but don't count on it.)

Comment 2: For a kinder, gentler look at this issue, see: ***Huber v. Wells Fargo Home Mortgage, Inc., 248 S.W.3d 611 (2008).*** (The DIRT DD for 8/4/08.) (A lender that records a satisfaction of a mortgage within the time allowed by the state's mortgage payment statute is not liable for statutory damages, despite the fact that the lender did not "deliver" the satisfaction to the mortgagor as required by the statute.)

MORTGAGES; ESCROWS; PREEMPTION: Federal savings and loan regulation preempts state law concerning requirements by savings and loan associations that their borrowers creates escrows for taxes and insurance, including questions of the lenders' obligation to pay interest on such escrows. ***Madsen v. Washington Mutual Bank fsb, 2008 UT 69, 2008 WL 4299622 (Utah 9/23/08).***

In 1964, Mr. and Mrs. Madsen financed the purchase of their home by borrowing money from Prudential Federal Savings and Loan Association under a real estate mortgage contract. Washington Mutual is the successor to Prudential to this contract. The contract obligated the Madsens to make monthly payments (in the amount of their yearly taxes and insurance divided by 12) into an account held by Prudential. The Madsens claim that they are entitled to interest on this money based on a common law accounting theory. The Madsens claim that the money in this account was held as a pledge and the common law required Prudential, as pledge, to account for any profits earned through the use of the pledge. In a previous decision, the Utah Supreme Court agreed that the money was a pledge. However, Prudential argued that federal law preempted the claim.

[The procedural history of the case is complex, but largely irrelevant to the holding of the court and is therefore omitted.] The Utah Supreme Court held that the Madsen's claim was preempted by federal law. Prudential offered evidence of three federal statutes that exempted Prudential from payment of interest unless state law or the contract between the parties stated otherwise. Utah has no statute that requires interest to be paid on these accounts nor did the contract require interest payments to be made. As such, the federal law preempted the state contract law claim.

The Madsen's argued that the Utah Supreme Court and the Tenth Circuit had previously held that the claims were not preempted. However, the Utah Supreme Court rejected this argument-and noted that the issue was not before the Utah Supreme Court previously and that the Tenth Circuit dismissed Prudential's federal court claim because there was no "federal question" jurisdiction.

The court noted that even if the federal rules specifically permitting escrow accounts had not been in effect, the general supervisory authority of the federal regulatory agencies charged with responsibility over federal savings and loan associations (which have changed over time), together with general rules validating their mortgage lending practices would have justified the conclusion that state law was preempted.

Comment: This case dates back thirty years. The plaintiffs lost a million dollar verdict with decades of accumulated interest.

MORTGAGES; FORECLOSURES; JUDICIAL FORECLOSURE; JUDICIAL CONFIRMATION: In actions to confirm a foreclosure sale, the court's standard for confirmation must be whether the sales price is equal to or exceeds the true market value of the property, and not the "shock the conscience" standard used in an equity action brought to set aside a foreclosure sale (*i.e.* whether the sale was fairly conducted and whether any disparity existed between value and sales price such as to "shock the judicial conscience"). ***Cartersville Developers LLC v. Georgia Bank & Trust, 292 Ga. App. 375, 664 S.E.2d 783 (Ga. Ct. App. 2008).***

Bank purchased townhomes built by developer pursuant to a foreclosure sale and hired a real estate appraiser to value the townhomes. Appraiser arrived at its values by making taking into account the fact that the properties were in foreclosure, leading to a lower appraisal. In fact, the appraiser discounted each townhome by $10,000. The appraiser stated specifically that the market value of properties in foreclosure is lower than others. The bank's bid came it at just over these values, and it bought all of the townhomes at the sale.

At the judicial confirmation hearing, mortgagor/ developer objected to this approach. Its own appraiser estimated the value of the townhomes at around $20,000 more than the bank's appraiser. The trial court concluded that its only obligation was to determine if its "judicial conscience was shocked" by any disparity between the foreclosure sales price and the true market value per *Darby & Assoc. v. Federal Deposit Ins. Corp.*, 141 Ga. App. 78, 232 S.E.2nd 615 (1977). Darby had been a case in which a mortgagor attempted to set aside a foreclosure sale due to inadequacy of price. The court concluded in that case that the court must conclude that there has been some procedural inadequacy and, in addition, that the price was such as to "shock the judicial conscience."

The appeals court disagreed with the use of this standard. It pointed out that a different standard must be applied by trial court in an action by a lender to confirm a foreclosure sale. A trial court cannot confirm a foreclosure sale unless it its satisfied that the property sold brought at least its "true market value."

"True market value "is the price that the property will bring when it is offered for sale by one who is not obligated, but has the desire to sell it, and is bought by one who wishes to buy it, but is not under a necessity to do so . . .

Based on this definition, this court has previously found that a trial court erred by confirming a foreclosure sale based upon "evidence of the 'quick sale' value of the subject property because such a valuation does not reflect the price that would be obtained in a sale under the usual market conditions. . . ."

The court expressly disapproved of applying the standard in *Darby* in actions to confirm a foreclosure sale where the evidence demonstrates that the sales price is not at least as much as the true market value of property. It vacated the order of the trial court and remanded.

Comment 1: Certainly the appraiser should not have stated the case as we have seen. The market value of the properties should not be discounted simply because of the presence of a foreclosure. But some courts, on similar facts, have taken into account that the price produced at the sale is a cash auction price and necessarily is likely to be lower than what might be the price if the owner had months to sell and served cookies at open houses. Note that the only thing that happened here is that the *Darby* test was disapproved and the case remanded. But the quote of what ought to be the "fair market value" test certainly suggests that the "distress sale" character of the price bid at the sale ought not to be taken into account.

Comment 2: The primary function of the confirmation sale in most jurisdictions is just to set up a deficiency judgment. In light of that, the editor isn't troubled by the court's insisting on limiting the deficiency to an amount between fair market value and debt, since, after all, the foreclosure lender that buys at the sale will be able to use open houses and cookies to resell the property. Maybe even toasters!!!

MORTGAGES; INSURANCE; CANCELLATION: Under standard mortgage clause providing that mortgagee cannot cancel mortgagee in the event of "increase in hazard, change of ownership, or foreclosure" not known to mortgagee and requiring mortgagee to give insurer notice of "increase in hazard," the fact that a foreclosure has been initiated is an "increase in hazard" and if the mortgagee fails to notify the insurer, the insurer may refuse to cover mortgagee's loss caused to damages due to fire while foreclosure is still pending. ***U.S. Bank, N.A. v. Tennessee Farmers Mut. Ins. Co., 2007 Westlaw 4463959 (12/27/07) (appeal granted 5/27/08).***

A residential mortgage went into default, and the mortgagee initiated a non-judicial foreclosure. Tennessee has a "rapid fire" three week, three notice foreclosure procedure. Although there is statutory redemption in the mortgagor under the statutes in such cases, the statutes also permit waiver, which typically occurs.

The mortgagor filed for bankruptcy and stayed the foreclosure. Then the house was destroyed by fire. The insurer refused to pay the mortgagee's claim for the proceeds to be paid to it under the mortgage clause in the policy because, it claimed, the event of foreclosure was an event creating an increased risk to the insurer of which the mortgagee had a duty to notify the insurer.

Here is the relevant language of the policy:

"[Insurer] will:

(a) protect the mortgagee's interest in the insured building. This protection will not be invalidated by any act or neglect of any insured person, breach of warranty, increase in hazard, change of ownership, or foreclosure if the mortgagee has no knowledge of these conditions;

(b) give the mortgagee 10 days notice before cancelling this policy.

Mortgagee's Duties

The mortgagee will:

(a) furnish proof of loss within 60 days if the insured person fails to do so;

(b) pay upon demand any premium due if the insured person fails to do so;

(c) notify us of any change of ownership or occupancy or any increase in hazard of which the mortgagee has knowledge;

(d) give us the right of recovery against any party liable for loss; but giving us this right will not impair the right of the mortgagee to recover the full amount of the mortgagee's claim;

(e) after a loss, permit us to satisfy the mortgage requirements and receive full transfer of the mortgage."
The language requiring the mortgagee to notify the insured of any change of ownership or occupancy or any increase in hazard tracks almost verbatim a Tennessee statute, TCA Sec. 56-7-804, but says "increase of hazard" rather than "increase in hazard." The court found this distinction meaningless, and interpreted the application of both the policy and the statute.

The court indicated that there is some disagreement in the precedent on the point of whether a foreclosure action increases the "moral" risk to the insurer in that it increases the possibility that a fire will occur. The court cited cases in Alabama, Illinois and Indiana for the proposition that there was no increase in hazard and no duty to notify. It cited cases in Arizona and Kansas that concluded that the event of foreclosure does increase the hazard to the insurer, but noted that in most cases so holding the policy expressly required notice of a pending foreclosure, and not just a general requirement for notice of an "increase in hazard."

The court cited and quoted from a 2003 Kentucky case that noted that, while foreclosure might increase the risk to a degree, it may not "substantially increase the risk," which was required under the policy to trigger a duty to notify. Like many of the other cases, the Kentucky decision emphasized that insurance policies are to be construed in favor of the insured and against the insurer.

There was even a Sixth Circuit Federal Court of Appeals decision in which the policy required notice of foreclosure, but the court remanded for an interpretation of whether this meant "initiation" of foreclosure or "completion." The trial court, on remand, found that it meant "conclusion." Nevertheless, the Sixth Circuit had, in its discussion, concluded that foreclosure does create an enhanced risk of loss to the insurer. The court found this discussion helpful:

"With the structure of the standard mortgage clause in mind, we turn to interpretation of the term "increase in hazard," used in the list of conditions that the mortgagee is required to report to the insurer, as well as in the list of conditions listed as exceptions to the insurer's promise not to invalidate the protection of the mortgagee's interest in the insured property. The issue is whether the commencement of foreclosure proceedings constitutes an "increase in hazard," which the mortgagee is required to report to the insurer or risk invalidation of its protection under the policy. We are mindful of the caselaw finding that the initiation of foreclosure proceedings is not necessarily an "increase in hazard," reasoning that the insurer could have explicitly used the phrase "commencement of foreclosure" if that was its intent. Nevertheless, we are persuaded by the numerous cases observing that the increase in hazard associated with the initiation of foreclosure proceedings is "universally recognized." . . . We agree with the Sixth Circuit's observation . . . that the initiation of foreclosure proceedings creates a substantial increase in the risk of fire loss because it gives the financially delinquent insured "incentive to destroy the house intentionally to receive the proceeds of the insurance policy" to apply against his debt. . . . Certainly an increased risk of fire arises at "such time as the insured has knowledge that the foreclosure proceedings have actually been commenced, and that he is about to lose his property.". . . Under the mortgage clause, the Bank had a duty to notify Tennessee Farmers of the "increase in hazard" when it informed Hill that it was initiating foreclosure proceedings. Likewise, because the Bank did not notify Tennessee Farmers of this fact, this would fall under the stated exception to Tennessee Farmers' assurance that the Bank's protection under the policy would not be invalidated "by any ... increase in hazard ... if [the Bank] has no knowledge of [this] condition [ ]...." (Citations omitted.)

Although the analysis of the statute was somewhat more convoluted, and affected by Tennessee precedent, in the end the court reached basically the same conclusion with respect to the meaning of the statute – the lender had the duty to notify the insurer of the initiation of foreclosure and, in failing to do so, it denied the insurer the opportunity to withdraw coverage if it saw fit, as it had a right to do under the policy and statute. Consequently, on remand the trial court should consider that the insurer had the right to refuse to cover the mortgagee's interest here.

Comment 1: The editor is indebted to Tennessee bar member, and raconteur, Coburn Dewees Berry, IV, who discussed this case at a Tennessee Land Title Association program that the editor attended. It was the editor's impression that many in the audience, like the editor, were surprised by the outcome here and would have concluded that the interpretive presumption against the insurer would have reached a different result.

But we didn't have the advantage of the precedent that the court did in this case. It does appear that insurers have been able to convince courts that the institution of foreclosure is an invitation to borrowers to torch their home. Interesting. And surprising.

Comment 2: The editor suspects that many lawyers in the foreclosure business also will be surprised by this outcome, and thus the situation becomes a malpractice trap for some of them. This may be a matter routinely covered on the checklist of a servicer in preparing for foreclosure, but it doesn't appear to have been on this servicer's checklist, and consequently the lawyer may have a responsibility to put it there.

Note: The Tennessee Supreme Court granted a writ of appeal on this case in May of this year, which the editor understands is somewhat unusual in real estate cases. But even if the outcome is reversed in Tennessee, the authority in other jurisdictions is still there and suggests that foreclosing lenders notify mortgagees or seek clearer language in the policy excusing such duty.

MORTGAGES; FORECLOSURE; INSURANCE: Under standard mortgage clause providing that mortgagee cannot cancel mortgagee in the event of "increase in hazard, change of ownership, or foreclosure" not known to mortgagee and requiring mortgagee to give insurer notice of "increase in hazard," the fact that a foreclosure has been initiated is an "increase in hazard" and if the mortgagee fails to notify the insurer, the insurer may refuse to cover mortgagee's loss caused to damages due to fire while foreclosure is still pending. ***U.S. Bank, N.A. v. Tennessee Farmers Mut. Ins. Co., 2007 Westlaw 4463959 (12/27/07) (appeal granted 5/27/08)***, discussed under the heading: "Mortgages; Insurance; Cancellation."

MORTGAGES; NOTES; STATUTE OF LIMITATIONS: In Mississippi, negotiable notes have longer statutes of limitations than non-negotiable, and therefore longer foreclosure periods. ***Jordan v. BancorpSouth Bank, 964 So. 2d 1205 (Miss. 2007).***

The foreclosing lender successfuly argued that the six-year statute of limitations in Section 75-3-118(a), which is part of Article 3 of the Mississippi's version of the Uniform Commercial Code, applied because the note was a negotiable instrument under Section 75-3-104. The county court held that the note was negotiable and that the longer six-year statute therefore applied. Jordan appealed, and the Mississippi Court of Appeals, in a decision by Justice Chandler, affirmed.

Reporter's Comment 1: This distinction between the statutes of limitations for negotiable and non-negotiable notes was created when Mississippi adopted the uniform version of Article 3 of the Uniform Commercial Code. The editor thinks that this is the first reported Mississippi case to recognize this distinction.

Reporter's Comment 2: There are a couple of reasons why real estate lawyers need to be cognizant of this distinction between negotiable and non-negotiable notes. A deed of trust cannot be enforced after the statute of limitations runs on the note it secures, accordingly, whether the note in negotiable and has a six-year statute of limitations, or whether it is non-negotiable and has a three-year statute of limitations, directly affects the enforceability of the deed of trust. One problem that this distinction creates is that under Section 89-5-19, a deed of trust loses priority to subsequent creditors and purchasers for value without notice when it appears from the face of the deed of trust that an action to enforce the indebtedness secured by the deed of trust is barred by the statute of limitations. But one looking at the face of a recorded deed of trust cannot tell whether the secured note is negotiable or non-negotiable, so he cannot tell for sure when the deed of trust begins to lose priority.

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

MORTGAGES; PREEMPTION: Federal savings and loan regulation preempts state law concerning requirements by savings and loan associations that their borrowers creates escrows for taxes and insurance, including questions of the lenders' obligation to pay interest on such escrows. ***Madsen v. Washington Mutual Bank fsb, 2008 UT 69, 2008 WL 4299622 (Utah 9/23/08),*** discussed under the heading: "Mortgages; Escrows; Preemption."

MORTGAGES; SUBROGATION; FRAUD: Fraud victim who advances money to pay senior mortgage may not acquire subrogation as against subsequent purchaser of property at foreclosure of junior mortgage. ***Casstevens v. Smith, 2008 WESTLAW 4660152 (Tex. App. 10/23/08).***

This little case doesn't make any major decisions of law, but certainly is an interesting story and stands as useful precedent for a number of minor points of law, and is worth noting for those reasons.

Carrolls and Casses [abbreviated names] were next store neighbors. Carrolls convinced Casses to purchase Carroll's home on a seller financing arrangement. Cass paid $34,000 in cash and executed a note for $90,000 for a warranty deed. Casses did not seek title insurance or otherwise check title. If they had, they would have discovered that Carrolls owed $88,000 on a prior bank mortgage and around $18,000 on a junior purchase money mortgage to Campbells – the prior owners of Carroll's home.

For some time, Casses made payments to Carrolls, and Carrolls apparently passed on some of the money paid to service the bank loan, and perhaps some on the Campbell loan. But the, in 2004, Casses discovered the existence of the bank loan. In one of the slickest scams likely to have occurred in that Texas neighborhood in a while, Carrolls convinced Casses to prepay the bank mortgage by giving $64,000 to the Carrolls. The Casses gave this money to the Carrolls, but Carrolls simply kept it and never paid down the bank loan.

In less than a year, the Campbell loan was in default and foreclosed. The amount of the lien had increased – probably through accumulated interest on unpaid debt – to $22,000, and a third party, Smiths – bought the property at a non judicial foreclosure sale.

Smiths sent a notice to the Carrolls at the residence address notifying them that they had acquired the property and seeking to make arrangements to take possession. This letter apparently was opened by the Casses, who learned for the first time of the second loan to Campbells. There ensued a series of negotiations. Casses believed that Smiths were willing to let them refinance and ultimately pay off Smiths and preserve their home. Smiths, however, at least in the end, were open only to a lease arrangement. Smiths ultimately paid off the $44,000 then owing on the bank mortgage.

Casses, of course, got a fraud judgment against Carroll, but this likely was uncollectable and anyway didn't solve their problem with Smiths. Ultimately failing to get what they wanted in negotiations, they went to court. The trial court entered a summary judgment for defendants, and the appeals court affirmed in significant part. The various holdings, some of them valuable as precedent, as indicated, although minor in scope, are set forth below.

1. A Texas forcible entry and detainer action can be brought by a foreclosure purchaser entitled to possession, and not only by a landlord against a tenant. In essence, the court concluded, the Casses were "tenants" of the Smiths in that they had begun occupancy lawfully and peaceably but the Smiths now wanted them out.

2. Although Casses alleged that they had given monies to Carrolls that were paid over to the bank mortgagee, this did not result in a subrogation to that position for the Casses superior to the claim of the Smiths. The court does not comment on the obvious fact that subrogation typically is not available for a partial payoff in any event. It states (incorrectly) that subrogation is only available to protect the subrogee's rights as against the original debtor whom the subrogee paid. As we have seen often on these pages, mortgagee subrogation often is available to protect a refinancing mortgagee against a junior mortgagee in the same property. It was unwilling to permit Casses to obtain subrogation against the Smiths.

Another problem for Casses is that Smiths bought without knowledge of the fraud and in the expectation that they were liable to the existing bank lien. Casses did not thereafter make any payments, or have any payments made in their behalf, on that lien. Thus, the fundamental basis for equitable subrogation, unjust enrichment, doesn't exist.

3. The fact that Smiths got a bargain when they bought the property for $22,000 subject to a $44,000 lien – apparently less than half the value paid for it originally by the Casses, and perhaps substantially less than that because all this happened when home prices still were soaring – was not unjust enrichment. Although the Casses were treated unfairly, that wasn't the Smiths' doing. Casses were defrauded by their old neighbors, the Carrolls.

4. Various conciliatory statements made by Smiths in correspondence with Casses did not work a fraud – lulling Casses into a false sense of security while the Smiths were planning to pay off the first mortgage. Casses alleged that they would have purchased the first mortgage if Smiths had not led them on, but the court noted that this really would not have preserved their title. They would have just been the ones receiving Smiths' payoff. In any event, the statements made by Smiths were pretty standard statements of good faith negotiating position, and nothing more: "We desire to work with you to salvage something positive from this . . . wrongdoing by [Carrolls]" Smith did say: "If we work together, we might be able to do something about these prior liens," but this was at a time when Smith thought that there might be a title insurer with some liability here. He subsequently discovered Casses had not obtained title insurer or checked title. There was no fraudulent intent or effect in his statement.

The case went on to discuss, rather ambiguously, an allegation that the Smiths may have violated a fair debt collection statute by asking an employee to bring the eviction action in her own name, rather than that of their company. The court acknowledges that there may be some basis for finding a violation, but doesn't seem to view it as very serious. Of course, we don't have all the evidence on this issue as yet.

Comment: The discussion of subrogation is perhaps the most substantial part of the case. But, as noted, the editor believes that the court was right for the wrong reason. Even if the Casses had paid off the senior mortgage in full, they couldn't get around the fact that Smiths bought on the basis of current record information concerning the mortgage. If they had paid it off, the mortgage would have been cancelled at the time that Smiths bought. Consequently, there could be no subrogation against them, as they relied on a clean record. The essence of the subrogation argument is that a party who is already junior to an existing lien might be unjustly enriched as against a third party who pays it off without realizing that the junior interest might then elevate to senior status.

OPTIONS; PURCHASE PRICE: An option to purchase in a lease is valid notwithstanding the fact that it does not set a specific price, but only "fair market value," where the option states that the price will be established by arbitration if the parties cannot agree on a price. ***Meridien Hotels, Inc. v. LHO Financing Partnership I, L.P., 255 S.W. 3d 807 (Tex. App. 2008).***

OPTIONS; REFUSAL RIGHTS; GIFTS: While a transfer of property for less than fair market value is not a gift, and can be a "sale" triggering a refusal right, the offer to carry out such a purchase will not satisfy the "bona fide offer" test typically appearing in such rights if the offeror is aware that he is paying less than fair market value. ***Schroeder v. Duenke, ___ S.W.3d ___, 2008 Westlaw 3844741 (Mo. App. 8/19/08).***

In August 1980, certain individuals ("Sellers") conveyed title to a five-acre parcel of land to Harold and Eleanor Duenke by general warranty deeds. That parcel was carved out of and contiguous with land retained by the appellants. Eight days after the conveyance, the Duenkes granted the Sellers the right of first refusal to purchase the tract, which was recorded along with the warranty deeds in September 1980. The Duenkes lived on the property until 1996, at which time they conveyed the property to their son ("Son") for $85,000 ($60,000 of which was borrowed). An appraisal completed in 1996 valued the property at $125,000.

Several years later, Son listed the property on the open market for $250,000. One of the Sellers noticed a "for sale" sign, which prompted him to check the public records and discover the conveyance between the Duenkes and Son. During the trial, the Sellers contended they "would have been able and willing to purchase the Property on the same terms," had they been aware of the 1996 transfer to Son. The Sellers sued for specific performance of the right of first refusal and quiet title. At trial, the court found that the 1996 transfer to Son did not trigger the right of first refusal because it was "an "intra-familial transfer" akin to a gift, and [] was not based on a 'bona fide offer' and 'sale' because (1) the Property was not listed for sale on the open market; (2) [the Duenkes] accepted whatever [Son] could afford; and (3) they accepted a price that was below fair market value so as to keep the Property in the family." Sellers appealed.

On the issue of whether the transfer was akin to a gift, the Missouri Court of Appeals first noted the Missouri principle that "a transfer of property by gift from one family member to another does not trigger a right of first refusal." However, the Missouri Supreme Court has defined an inter vivos gift as "a voluntary transfer of property by the owner to another, without any consideration or compensation as an incentive or motive for the transaction," and "a voluntary and gratuitous assignment of something by one without compensation to another who takes it without valuable consideration." In light of that cited case law, the court held that the 1996 transfer to Son was not a gift, because (1) Son financed $60,000 of the purchase price, (2) Son paid $85,000 in consideration for the property to the Duenkes, and (3) the warranty deed executed in conjunction with the 1996 transfer to Son specifically stated it was in exchange for valuable consideration. The court also distinguished the case relied upon by the trial court in which a transferee received property from her mother by way of gift, with no consideration paid.

But this analysis did not get the optionees to where they wanted to be – the court did not conclude that the trial court should have granted optionees' motion for summary judgment. Rather, the court concluded that genuine issues of material fact remained regarding whether Son's offer to pay the Duenkes $85,000 for the property was a "bona fide offer." With respect to this issue, the court noted that Missouri law does not require the property in question to be placed on the open market, and the fact that the parties intended to keep the property in the family has no bearing on the question. But the court cited another element: a bona fide offer must be based on fair market value, which is a determination ordinarily made by the finder of fact. Here, the fact that the 1996 transfer to Son was at a price $40,000 less than the appraised value was not enough to establish that the price was not based on fair market value. Accordingly, the case was remanded for submission of the question of "bona fide" offer to the jury.

Comment 1: Typically the refusal right is triggered by a "sale" of the property, and a number of cases have dealt with the definition of "sale" to require that a price actually be paid. But, like the instant case, these cases do not appear to contemplate that the "sale" in question be for fair value, only that value transfer as part of the bargain. *Cottrell v. Beard,* 9 S.W.3d 568 (Ark. Ct. App. 2000) (the DD for 9/27/00) Note that in this case the court dealt primarily with whether the transfer could be excluded from the definition of sale because it was a "gift," without really spending much time defining what was a "sale."

Compare *(1) Park Station Limited Partnership, LLLP v Bosse,* 378 Md. 122, 835 A. 2d 646 (Md. 2003) (The DIRT DD for 1/ 20/04) (Donation of property to a nonprofit foundation does not trigger refusal right even though a motivating factor might be the tax write-offs to be obtained from such donation, because transfer is not a "sale." (Citing other cases involving gifts from other jurisdictions also finding that the refusal right is not triggered) (2) *Hartzheim v. Valley Land & Cattle Co.,* 62 Cal. Rptr. 3d 815 92007) (The DIRT DD for 7/27/07) (A probate planning exchange of property, structured as a for value exchange, in which grandchildren of principles of LLC landlord/optionor trade their interests in other property for interests in property owned by LLC, does not trigger right of first refusal held by tenant of LLC in the property in which grandchildren have acquired their interest, but the refusal right is not destroyed and remains applicable to land in hands of grandchildren.)

Comment 2: If the transfer was a "sale," then how could the son's agreement to purchase the property for $85,000 not be a "bona fide offer" as intended by the parties to the original agreement? It certainly was appropriate to reverse summary judgment for the optionors, but was it really appropriate to conclude that there was a "genuine issue of material fact" requiring submission to the jury? The problem may lie in the precedent, which the court concluded required that any offer be "based upon the fair market value." The court concluded that the son could afford to pay what he paid, and had an awareness of the value of the property, but may have paid less than the appraised value of the property, and that therefore his offer did not satisfy the "*bona fide* offer" test.

The consequence of such an analysis is that optioners subject to rights of refusal phrased so as to require *bona fide* offers (which is very common language) can circumvent the right of refusal by selling for a lesser amount to persons to whom they owe some moral obligation or non-monetary consideration. One assumes that the right of refusal remains in effect. In this case, however, the optionees argued that they couldn't afford to match the latest offer – $250,000 – and should have had a chance to match the son's offer.

Certainly an offer for *more* than the fair market value might not be *bona fide*, if the sole purpose is to force the optionees to either exercise their right or forfeit it. But can the same be said for an *under* market right? Perhaps it depends upon what the parties intended, or, better, how their counsel phrased their intent.

RECORDING ACTS; BONA FIDE PURCHASERS; TAX FORECLOSURE REDEMPTION RIGHTS: Corporation claiming title to property by the right of redemption under a 1982 tax deed purchased in 2006 was good faith purchaser for value without notice of interest of individual purchaser of property pursuant to a 1990 tax deed when there was no record evidence that all proper steps to foreclosure of those rights had been completed by the individual purchaser. Individual owner, in any event, did not establish satisfaction of all requirements of foreclosure of prior redemption rights. Individual purchaser's occasional clean up and mowing of property and payment of public authorities for more clean up and demolition of buildings did not establish actual possession of the property under four year adverse possession statute available in such cases. ***Washington v. McKibbon Hotel Group, Inc., 284 Ga. 262, 664 S.E.2d. 201 (Ga. 2008),*** described under the heading: "State and Local Taxation; Property Tax; Tax Foreclosure; Redemption; Foreclosure."

STATE AND LOCAL TAXATION; PROPERTY TAX; EXEMPTIONS; HOSPITALS: Although the term "hospital purposes" is not defined in New Jersey's real property tax exemption statute, it does not only mean a place where a patient can obtain twenty-four hour continuous care and could include any location where hospital patient medical services, such as pre-admission or post-admission services are provided. ***Hunterdon Medical Center v. Township of Readington, 195 N.J. 549, 951 A.2d 931 (2008); July 14, 2008.***

TAXATION; PROPERTY TAX; EXEMPTIONS; UNIVERSITIES: A public university does not bear the burden to show a public purpose for its family housing to qualify for exemption from real property taxation and, alternatively, the statutory authority granted to a public university demonstrates that the family housing serves a public purpose. ***Stoddard v. Rutgers, 24 N.J. Tax 187 (Tax Ct. 2008)***

A property taxpayer sued to invalidate a local property tax exemption to a state university for apartment buildings used by university graduate students and their families. The taxpayer alleged that taxpayers in the municipality had been unfairly burdened with the costs of providing children living in the school's family housing with free public school education because of the lack of tax ratables for that housing.

The Tax Court reminded the parties that all actions challenging tax exemptions must comply with all applicable statutory requirements.

The university filed a motion to dismiss for failure to state a cause of action. It argued that as public entity it did not bear the burden to show a public purpose for its family housing to qualify for exemption, and alternatively, the statutory authority granted to it demonstrated that family housing served a public purpose.

The Tax Court granted the motion to dismiss because it found no assertion of facts in the taxpayer's pleadings that the family housing was not integral to the mission of the university, or that the university was receiving profits being used for other avenues other than purposes that had been statutorily authorized. It also found no facts alleged in the taxpayer's complaint that would lead to the conclusion that the family housing was not operated for legitimate university purposes which would qualify for tax exemption under law.

STATE AND LOCAL TAXATION; PROPERTY TAX; VALUATION: Taxpayer, owner of a catering facility, loses both on the issue of "entrepreneurial profit" and on the issue of deducting for "functional obsolescence" due to lack of parking. ***Westwood Lanes, Inc. v. Garwood Borough, 2008 WL 3854462 (Tax Ct. 2008)***.

A catering facility challenged its tax assessment. The catering facility and the municipality each retained experts to calculate the property's value. Both experts relied on a "cost approach" to value. The catering facility's expert did not include "entrepreneurial profit" as a factor in measuring the property's value, whereas the municipality's did.

Entrepreneurial profit is a measurement of the profit a property owner would receive for its renovations to the property in anticipation of a resale and the associated risk. The catering facility's expert claimed that there was no entrepreneurial profit to be inferred for the property since it was custom-built as a catering hall and catering facilities are not constructed with the expectation of resale profit.

The opinion is useful to researchers and to others dealing with the question of "entrepreneurial profit" both because of the court's thorough discussion of the issue and also because of its ten page charge analyzing other cases in New Jersey discussing the issue.

In the end, the Tax Court rejected the catering facility's argument, finding that the catering facility's location in an expanding commercial district gives rise to an inference of entrepreneurial profit. It concluded that anyone buying the property would take into account the possible value that might be obtained by remodeling and reselling, and would not rely exclusively on potential revenues from catering operations as a basis for computing value. Therefore, the Tax Court found it reasonable to conclude that renovations made to the property were made in anticipation of realizing a profit when the property was resold. Since the catering facility did not calculate entrepreneurial profit, the Tax Court relied on the municipality's calculation instead.

The Tax Court then reviewed the competing calculations for functional obsolescence. Functional obsolescence is a measure of calculating the diminution in value of a property that is caused by a flaw in the structure, materials or design of the property, when compared with its best use and most cost- effective design. Functional obsolescence may be curable or incurable. In this instance, the owner argued catering facility was functionally obsolete because it lacked sufficient parking, leading to "economic obsolescence." However, insufficient parking may be cured by either leasing or purchasing a neighboring property, as the catering facility did when it leased the neighboring property. When valuing the diminution in a property's value due to functional obsolescence, one can calculate it using either a replacement cost method or a reproduction cost method. In this case, however, the catering facility calculated the diminution in value by deducting the cost of purchasing the neighboring property.

The Tax Court found that the catering facility's calculation made no sense because it resulted more than a thirty-three percent diminution in value. It refused to accept the proposition that the property, if used as a catering hall, would be worth about $1,800,000 less than its worth for a different purpose. In addition, the Tax Court found illogical that, prior to acquisition of an adjoining property for a parking lot, the catering facility property would be worth about $3,000,000, but that after buying the adjoining property, its property would be worth about $4,800,000, while, in addition the catering facility would then own the adjoining property valued at about $1,650,000. If this were true, then clearly the "highest and best use" of the property would not be as a catering hall – an assumption that underlay the landowner's appraiser's earlier computations on other elements of the appraisal.

Comment: Although anything with numeric calculations, which appear throughout this opinion, is beyond the editor's pay grade, the editor found the two issues discussed above sufficiently engaging to study the opinion for a little additional education. Although the landowner got creamed in this case, study of the concepts and techniques may assist in dealing with appraisal evidence in a variety of other concepts, not the least of which, of course, is a tax appraisal.

STATE AND LOCAL TAXATION; PROPERTY TAX; ASSESSMENTS; UNIVERSITIES: A public university does not bear the burden to show a public purpose for its family housing to qualify for exemption from real property taxation and, alternatively, the statutory authority granted to a public university demonstrates that the family housing serves a public purpose. ***Stoddard v. Rutgers, 24 N.J. Tax 187 (Tax Ct. 2008).***

A property taxpayer sued to invalidate a local property tax exemption to a state university for apartment buildings used by university graduate students and their families. The taxpayer alleged that taxpayers in the municipality had been unfairly burdened with the costs of providing children living in the school's family housing with free public school education because of the lack of tax ratables for that housing. The Tax Court reminded the parties that all actions challenging tax exemptions must comply with all applicable statutory requirements. The university filed a motion to dismiss for failure to state a cause of action. It argued that as public entity it did not bear the burden to show a public purpose for its family housing to qualify for exemption, and alternatively, the statutory authority granted to it demonstrated that family housing served a public purpose.

The Tax Court granted the motion to dismiss because it found no assertion of facts in the taxpayer's pleadings that the family housing was not integral to the mission of the university, or that the university was receiving profits being used for other avenues other than purposes that had been statutorily authorized. It also found no facts alleged in the taxpayer's complaint that would lead to the conclusion that the family housing was not operated for legitimate university purposes which would qualify for tax exemption under law.

STATE AND LOCAL TAXATION; PROPERTY TAX; TAX FORECLOSURE; REDEMPTION; FORECLOSURE: Corporation claiming title to property by the right of redemption under a 1982 tax deed purchased in 2006 was good faith purchaser for value without notice of interest of individual purchaser of property pursuant to a 1990 tax deed when there was no record evidence that all proper steps to foreclosure of those rights had been completed by the individual purchaser. Individual owner, in any event, did not establish satisfaction of all requirements of foreclosure of prior redemption rights. Individual purchaser's occasional clean up and mowing of property and payment of public authorities for more clean up and demolition of buildings did not establish actual possession of the property under four year adverse possession statute available in such cases. ***Washington v. McKibbon Hotel Group, Inc., 284 Ga. 262, 664 S.E.2d. 201 (Ga. 2008).***

This is one of those cases where everything is fine and fits together until you read the dissent, and then you wonder whether both parties can possibly be talking about the same case.

Kearse, the owner of certain property, .082 acres, suffered a tax foreclosure, and Layton purchased at the tax foreclosure sale in 1982. Two years later, Layton suffered a tax foreclosure, and Shedrick acquired the property at a tax foreclosure sale in 1984. Six years later, Shedrick suffered a tax foreclosure sale, and Washington bought at this tax foreclosure sale, in 1990.

Georgia law recognizes a statutory right of redemption in the foreclosed landowner at a tax foreclosure, and like many jurisdictions, places the onus of terminating the right of redemption upon the foreclosure sale purchaser, who must institute a procedure to terminate the statutory redemption right. In the alternative, the tax sale purchaser is given an abbreviated four year statute of limitations in which to acquire good title against the foreclosed owner through adverse possession.

Washington apparently intended to cut off the foreclosed owner's right of redemption, and apparently did have a sheriff post a notice on the abandoned shack that stood on the property, which was the last known address of the prior occupant. Washington also published notice. Washington had no knowledge of the location of any of the prior owners of the property, although it is unlikely Washington was aware that he should have notified any of them. What else, if anything, Washington was supposed to do, but allegedly didn't do, we don't know. The dissent and the majority seem at odds as to the adequacy of Washington's acts. But Georgia law also provides that notices required by the redemption cutoff statute "may be filed . . . and recorded . . . ." According to the dissenter, "[t]his statutory provision does not mandate that the completion of the foreclosure process be documented on the county real estate records."

In any event, as we'll see, Washington's failure to record proved problematic.

In 2006, Mkibbon, the owner of adjacent hotel property, acquired the 22 year old redemption right of Layton (remember that he preceded in title Shedrick, who bought at the foreclosure sale of Layton's title.)

The trial court held that Mkibbon's redemption rights were valid and could be exercised against Washington because they had not been cut off. The court deemed it irrelevant whether Washington in fact complied with the notice requirements of the cutoff statute, because the trial court held that "since the documentary record is silent as to any actions taken by [Washington]" in regard to cutting off redemption, Mkibbon "stands in the position of a good-faith purchaser for value without notice."

The court then perforce had to turn to Washington's alternative claim that he cut off any redemption rights by adverse possession during the period since 1990. Only four years of adverse possession is required by Georgia's statute on cutting off redemption. Washington had paid taxes every years since 1990, but the court deemed that as inconsequential, because the paying of taxes does not involve a possessory act. Washington also cut the grass and brush and cleaned up the property generally two or three times a year. The local county tore down the old shack on the property and cleaned up the property itself from time to time. The trial court did not deem this activity to be an act of possession by Washington, but the county wasn't shy about demanding that Washington pay for its services in this regard, which, according to the dissent, he did.

The Georgia Supreme Court affirmed the trial court, subject, as noted, to a stinging dissent from Justice Benham, which, obviously, the editor finds convincing.

Comment 1: As the dissent notes, there are two conflicting public policies here.

There is the policy of protecting landowners from the consequences of a relatively harsh procedure of collecting taxes through foreclosure sale – thus a generous right to redeem. This right was so generous that it was available for purchase 22 years after it arose. Wow!!

There is also the policy on insuring finality for foreclosure sale purchasers to clear the title to the property and keep the property in the market – thus the short adverse possession statute. In fact, as the dissent notes, only about fifty years ago the Georgia General Assembly provided that title to tax foreclosed property ripened into good title after a passage of time, without reference to whether adverse possession had occurred, but this provision was later amended.

Comment 2: The editor definitely is puzzled about the "permissive language" argument by the dissent. Sounds right. But are all recording acts provisions written in a similarly permissive way? Recording is never a condition of validity. Thus, the court's treatment of the cutoff of redemption here may be consistent with other recording act results.

Nevertheless, the editor would expect to find more specificity about buyers being able to rely upon failure to record notices cutting off redemption rights before the editor would conclude that the Georgia legislators truly intended that result. The Georgia court appears to be writing on a blank slate here. The cases it cites aren't really on point. As indicated, the editor finds the dissent compelling based upon this record. What a maverick!!!

STATUTE OF FRAUDS; VENDOR/PURCHASER: The Statute of Frauds can provide a Seller with a complete defense to a contract for the sale of real estate even when the most material terms have been orally agreed upon for nearly two years but the parties have not yet reached an agreement on several less fundamental matters. ***Moorman v. Blackstock, Inc., 661 S.E.2d 404 (Va. 2008)***, discussed under the heading: "Vendor/ Purchaser; Statute of Frauds."

STATUTE OF LIMITATIONS; INSTRUMENTS UNDER SEAL: Although a note secured by a deed of trust is not executed under seal and is subject to a three year statute of limitations, if the deed of trust contains a separate promise to pay the same debt and is executed under seal, the twelve year statute of limitations applicable to sealed instruments will apply. ***The Wellington Company, Inc. Profit Sharing Plan and Trust v. Shakiba, 180 Md.App. 576, 952 A.2d 328 (2008).***

On October 12, 2005 Lender filed suit to collect on a commercial note secured by a deed of trust on real property. The note was a balloon note (carrying 18% interest) and was due on May 1, 2002. Borrower claimed that the three years Statute of Limitations in Maryland on actions in contract barred the claim and moved to dismiss. The motion was denied and the case went to trial.

At trial, it developed that the property covered by the deed of trust had been foreclosed by the holder of a senior lien, wiping out the deed of trust. Lender's witnesses were uncertain whether a deficiency had been sought as a consequence of that foreclosure, and the court appeared to assume that there had been no such deficiency claim.

Lender argued, nevertheless, that it was entitled to recover on the note because it was a "specialty" under Maryland law – a sealed instrument – and therefore entitled to a twelve year limitations period. Borrower responded that there was no seal on the note, but Lender argued that the signature block contained the legend "signed, sealed and delivered," and that under Maryland law the simple statement that an instrument is sealed is sufficient to accomplish a seal, and that no formal seal is necessary.

The court disagreed. It acknowledged that all that might be necessary under Maryland law might be for the word SEAL to be printed on the document, without any other kind of formal seal, but held that a mere recitation that the instrument is sealed is not enough to invoke the benefits of a sealed instrument. The court also pointed out that the recitation in the note stated that the seal was witnessed, and that there was a signature block for the witness signature, but no signature appeared.

But, the lender persisted, the deed of trust in this case was indisputably under seal, and contained a separate promise to pay the debt, and thus provided sufficient basis for the lawsuit alone, and enjoyed the benefit of the longer statute of limitations. The trial court had rejected this argument, but it had more appeal for the Maryland intermediate appeals court.

The appeals court concluded that the promise to pay contained in the Deed of Trust and the existence in the deed of trust of an acknowledgment of the debt, read together, constitute a specific, definite obligation on the part of borrower. "The parties did not render this obligation unenforceable merely by reciting the same obligation in a second document, i.e., the Note . . . the Note and Deed of Trust are separate, enforceable contracts. Although [Lender] could not recover twice, it was entitled to seek repayment under either the Note or the Deed of Trust."

Borrower asserted that the sole remedy to collect the debt under either the note or deed of trust was an action for deficiency following the earlier senior foreclosure. It claimed that the specific statute authorizing deficiencies in such cases ought to be deemed exclusive. Although this argument convinced the trial court, it didn't work on appeal. The appeals court concluded that the purpose of the statute was to confer jurisdiction on a foreclosing equity court to enter a money judgment, and not to establish an exclusive remedy for collection of a debt represented by a contractual statement of obligation contained in the deed of trust. The court also dismissed arguments that the deed of trust, for these purposes, should be considered separately from a mortgage, because it specifically was made out to the trustee, rather than to the beneficiary. Because the deed of trust contained a promise to pay the debt owed to the lender, the fact that it was contained in a document creating a security interest through a trustee was of no consequence.

The court saw no inconsistency in permitting the Lender to recover on the debt set forth in an instrument other than in the note when an action on the note was barred. It doesn't really explain why this is so. The fact that Maryland has decided that a longer limitations period applies to action under seal seemed to be a sufficient answer. The court cited a number of authorities to the effect that special benefits accrue to a promissee when an instrument is under seal, and have so accrued for centuries.

Comment: Undoubtedly all of this is perfectly clear to east coast lawyers in traditional common law states such as Delaware and Maryland (and perhaps others) that elevate the significance of what is little more than a second signature on documents or even boiler plate in the document form to a sacred status. The editor understands that a certain amount of mysticism is always useful to impress the clients that their lawyers are effectively high priests dealing on a plane beyond that of mere mortals. But, in light of the fact that the seal is almost certainly legal gobbledygook that the party executing the documents (and the party receiving them) almost certainly does not credit as having special significance, the editor believes that its presence should not make a significant procedural or substantive difference in the rights of the parties.

On the other hand the editor doesn't like crab cakes so much either – can't stand the mayonnaise.

SUBDIVISIONS; EXACTIONS; OPEN SPACE: The Municipal Land Use Law gives a municipality authority to require contributions from a developer for off-tract water, sewerage, drainage, and street improvements, but does not authorize a municipality to extract monetary contributions for open space or recreational areas. ***New Jersey Shore Builders Association v. Township of Jackson, 401 N.J. Super. 152, 949 A.2d 312 (App. Div. 2008).***

TITLE INSURANCE; EXCEPTIONS TO COVERAGE; "PARTIES IN POSSESSION:" An exception for "rights of tenants or person in possession" removes from coverage all rights held by a tenant whose lease was not recorded, including a right of first refusal. ***326 4th Street Corp. v. Chicago Title Ins. Co., 2008 WL 4346417 (N.Y.A.D. 1 Dept. 2008).***

TITLE INSURANCE; MARKETABLE TITLE; ENCROACHMENTS: Although an insured in Arkansas may not be able to recover from a title insurer for an negligent title search, the insured will have a claim under marketability coverage when the insured land includes a building that projects into a public street based on an airspace lease that is not insured, which contains defects that are not excepted, the encroachment made title unmarketable, effectively providing coverage for the lack of a valid assignment of that lease. ***Chicago Title Ins. Co. v. Arkansas Riverview Development, LLC, ___ F.Supp.2d ___, 2008 WL 4004892 (E.D.Ark.).***

The Arkansas Bar Foundation sold its Little Rock building to Gary Canada, who assigned the contract to Arkansas Riverview Development, LLC. The deed described the property as platted lots and a vacated alley. The legal description in the title insurance policy issued by Chicago Title matched the deed.

The Foundation was either sloppy or forgetful. Its building had been allowed to project out over Garland Street based on a 1971 air rights lease from the City of Little Rock. The contract leading to the title insurance activity in this case said that Riverview would buy the land "together with all appurtenances thereto, including, without limitations, air rights." However, no assignment of the lease was prepared.

Riverview began refurbishing the building after closing. When it sought to build additional stories on top of the building, including in the airspace over Garland, Riverview asked for and received an assignment from the Foundation. However, the lease required prior consent of the City for an assignment and it also gave a neighboring hotel a right of first refusal. Riverview did not get the consent or waiver of the hotel's rights.

The Chief Executive Officer of the City Advertising and Promotion Commission sent a letter to the Foundation and Riverview saying that the lease had been violated due to the failure to get the City's consent before the "attempted conveyance" of the lease, because no notice had been given to the hotel, and because the proposed addition would violate a height restriction in the airspace lease.

This curious means of advertising and promoting the city was followed by a revocation of the building permit. Riverview sued the City of Little Rock and Capitol City Hotel Limited Partnership to enjoin the revocation of the permit, seek a declaration that the assignment of the airspace rights was valid, and to quiet title to the airspace rights. An injunction was issued, and then the dispute was settled. The building plans went forward, and the addition was allowed to go above the height restriction. Riverview paid the hotel money to release its right of first refusal. The City of Little Rock conveyed the airspace rights in fee simple to Riverview.

Riverview then made a claim on its title insurance policy for all of its expenses. Chicago Title denied the claim and filed a declaratory judgment action. Riverview counterclaimed for breach of contract and negligence. Chicago Title moved for summary judgment on both claims.

The federal court first ruled that Arkansas does not recognize a claim for abstractor liability on a title insurance contract. Riverview noted that the jurisdictions "are divided on the issue of whether a title insurer may be liable in tort for a negligent title search," citing Palomar, Title Insurance Law (which strongly advocates for such a claim). However, not in Arkansas:

"Although the Arkansas cases are not crystal clear, this Court is satisfied that it would be inconsistent with Arkansas law to impose tort liability on a title insurer for a deficient title search, at least in a case such as this where the plaintiff requested only title insurance and not a title report."

The court acknowledged that two Arkansas cases have held that there is a "duty on the part of title companies to make a reasonable search of the relevant records to detect clouds or defects in title." These are *Welch Foods, Inc. v. Chicago Title Ins. Co.,* 341 Ark. 515, 521, 17 S.W.3d 467, 471 (2000); and *Bourland v. Title Ins. Co. of Minn., 4* Ark.App. 68, 73, 627 S.W.2d 567, 570 (1982). However, neither said that "a violation of this duty creates liability in tort rather than for breach of contract." The court quoted Comment, Title Insurance: The Duty to Search, 71 YALE L.J. 1161, 1181 (1962), which said that "a court must be careful not to confuse the preliminary question of whether the insurer is liable for a negligent search with the later question of whether that liability is contractual or tortious in nature." In neither *Welch* nor *Bourland* did an insured bring suit for negligent misrepresentation of title.

The court also noted that, in Arkansas, a lawsuit on an abstract of title is a contract action, not a negligence claim. The same must be true of a claim against a title insurer, the court said. This distinction is important, because "the Supreme Court of Arkansas has held that negligent performance of an insurance contract is not a tort in Arkansas," citing a 2006 case. Also, the court said, negligent misrepresentation under Restatement (Second) of Torts § 552, which is the foundation for an abstractor liability claim, is not a valid cause of action in the state, citing a 1994 case.

Finally, Riverview tried to shoehorn its claim into one for "constructive fraud," which Arkansas does recognize. The court said that was not the claim Riverview pled, however, so it declined to address the issue. The court concluded by saying that title insurance is a contract of indemnity, no more and no less. The court did say that, if a separate title search contract had been made, the result "might be different." However, there was no such separate contract.

But the court took away Chicago Title's victory on the abstractor negligence issue when it considered whether there was coverage under the policy. Chicago Title's agent, had removed all standard exceptions from the policy, including the survey exception. Exception 3 in Schedule B recited two recorded amendments to the airspace lease, and a separate lease of a parking structure shared with the hotel. However, it did not except the original 1971 airspace lease, which was not in the chain of title. There was also a detailed exception for all of the encroachments shown on the survey provided to the agent at or before closing. Most telling, according to the court, was that "Chicago Title excepted all of the matters shown on the survey that might cloud title to Lots 4, 5 and 6 of Block 99 except the fact that the building was located partly on that tract and partly in the airspace above Garland Street."

The court said that, while "the issues are complicated and the parties have extensively discussed them in excellent briefs," most of the case boiled down to two issues: was title marketable when conveyed and, if not, "does the title insurance policy except or exclude the matter that rendered the title unmarketable?" The court answered the first question:

"The Court has no hesitation in saying that Arkansas Riverview Development did not have marketable title to Lots 4, 5 and 6 of Block 99 when the title insurance policy was issued. . . . "A marketable title is one that a prudent person with full knowledge of all of the facts would be willing to accept." . . . No prudent person with full knowledge of all of the facts would be willing to accept title to Lots 4, 5 and 6 of Block 99 with a building built partly on those lots and partly on adjacent property without also obtaining rights to the adjacent property. A person could not have peaceful enjoyment of such property."

It discussed a case in which the fact that a hotel's wall encroached onto neighboring land without right was found to render title unmarketable.

Chicago Title argued the difference between salability of the land and marketability of its title, and cited *First United, Inc. v. Chicago Title Ins. Co.*, 366 Ark. 508, 237 S.W.3d 15 (2006) for the rule that salability does not trigger policy coverage. In that case, a judgment in favor of time share interval owners would be imposed against a lender if it assumed ownership of the project on foreclosure. The Arkansas Supreme Court found that the lender would have the right to possess, control, and dispose of the property. The judgment made the property "unattractive to potential purchasers," but did not make title unmarketable.

Quoting from *First United*, this court found that Riverview "did not 'have the right to possess, control, and dispose of the property' because there were 'conflicting claims to the property,' i.e., the fact that someone else owned the right to the airspace above Garland Street where a large portion of the building was located. . . . Therefore, . . . the title was unmarketable."

The court acknowledged that, "[h]ad the standard exceptions not been removed, coverage might well be defeated by" the survey exception. The building in the street was shown on the survey. Chicago Title argued that "the fact that the building straddled the line does not mean that there was an encroachment," but rather was a non-covered trespass. The court again quoted Professor Palomar, from Patton and Palomar on Land Titles § 676, in finding that a building is an encroachment, and "[i]f the encroachment is substantial, it constitutes an encumbrance that justifies a purchaser in rejecting title." The court also used the policy and the company website against the insurer:

"The definition of encroachment on Chicago Title's website does not require that the construction onto the property of another be a trespass. … Because the policy does not define the term encroachment, and because the term encroachment can mean a trespass but also can mean construction onto the property of another even when there is no trespass, the term is ambiguous, so doubt as to its meaning must be resolved against Chicago Title."

The court thus construed the policy as being ambiguous for lack of a definition of a word that is found only in the very exception whose removal the court said created "coverage" in the first place. This is the circularity trap that is a common snare in survey exception cases. However, the court recognized the circularity, and held alternately that the marketability coverage was invoked no matter how the exception might be construed:

"Arguments about the meaning of the terms in [the survey] exception do not change the fact that Chicago Title insured that Arkansas Riverview Development had marketable title [or] that Arkansas Riverview Development did not have marketable title because it did not receive an assignment of the airspace rights on which a substantial portion of the building sat."

The court moved on to the long, detailed exception number 3 for lease rights between the city, the hotel and the Foundation, which it admitted created a "more difficult issue" about coverage. The court said the exception was not broad enough:

"The difficulty is that the original lease of the airspace rights from the City to the Bar Foundation, executed in 1971, is not listed in the special exceptions, but the 1973 amendment to and the 1994 extension of the original lease are."

Chicago Title argued that an exception for an instrument that refers to another instrument is sufficient to except both instruments, citing Arkansas law to that effect. Riverview cited another rule of contract interpretation, that the mention of one class of things implies the exclusion of all members of the class that were not mentioned. Again, it was Professor Palomar to the rescue for the insured: "[I]f a lien, encumbrance or other title defect is to be excepted from coverage, the title insurer must use clear, precise and unambiguous language in the exception." Palomar, Title Insurance Law, § 7:17:

"The special exceptions excepted the 1973 amendment to and the 1994 extension of the original lease but not the original lease; and they removed the standard exception for matters that would be shown by a survey and then excepted the matters shown on the survey without mentioning the elephant in the room-the fact that the building was built partly in the airspace above Garland Street pursuant to the original lease, which was not listed in the exceptions, and the 1973 amendment, which was. Because the special exceptions do not clearly, precisely, and unambiguously except the fact that the building was built partly on the tract that was conveyed and partly on a tract that was not conveyed, the special exceptions do not defeat coverage."

In the Reporter's view, Palomar's treatise overstates the actual holding of the cases interpreting the contract. For example, when a policy excepted an easement as being set forth in a mortgage, but not the easement itself, the exception was sufficient. *Sullivan v. Tomgil Building Corp.*, 260 N.Y.S. 2d 465 (Sup. Ct. 1965). See further cases recited in § 12.7.1, Title and Escrow Claims Guide. The court did not address such cases, although they were no doubt cited by the insurer in what the court admitted was an excellent brief.

The court also rejected other policy defenses. The real issue seems to have been whether or not Chicago Title consciously assumed the risk from Riverview that the building was an encroachment without right which the city could demand be removed. The excepted lease documents referred to the 1971 airspace lease. Nonetheless, the court made short shrift of Chicago Title's argument that this problem was "created" by the insured and thus fell under Exclusion 3(a):

"[Chicago Title argues] that Arkansas Riverview Development's problem was created by the failure . . . to comply with the requirements in the original lease that it obtain written consent from the City to assign the airspace lease and that it give a right of first refusal to the Camelot Hotel or its successors. Chicago Title characterizes these failures as "lease compliance problems" as opposed to defects in title … . However, the … title insurance policy contains no exception or exclusion for "lease compliance problems." . . . Chicago Title argues that . . . Arkansas Riverview Development elected to take an assignment of the lease to the airspace rights and agreed to undertake all of the obligations of the Bar Foundation pursuant to the lease, which then created the problems about which it now complains. Again, that is simply not true. What made the title to Lots 4, 5 and 6 of Block 99 unmarketable was the fact that the building on that tract also occupied another tract that was not conveyed."

The court did not even mention the definition of "land," which excludes any rights in adjacent streets. The court also said the post-policy exclusion did not apply because, it held, the marketability problem existed on date of policy and was not created by the defective assignment of air rights signed after the policy date. The court also found that Exclusion 3(b) did not apply, because the encroachment was disclosed to Beach Abstract by the survey. The court again implied that the risk of the lack of rights in the street was consciously transferred to Chicago Title simply by delivery of the survey.

Reporter's Comment: This decision is another example of how the marketability coverage can be used to manufacture "coverage" for rights that are not insured and which do not even exist, reading the limits of the insured estate or interest out of the policy. The court makes a valid criticism of the lack of a specific exclusion for disputes over the interpretation or enforcement of insured interests. The editor's draft policy form, introduced in the September issue, addresses these issues. If you are interested in participating in the project of drafting clarifying language for a proposed title insurance policy, please send an email to bnielsen@reinhartlaw.com to review the current draft of the policy on a title insurance claims website. The password-protected website also provides a user group forum for claims issues between claim administrators and retained counsel.

The Reporter for this item was Bushnell Neilson writing in his excellent Title Insurance Newsletter, which subscribers certainly can find out about by contacting Bush at his email address set forth above.

VENDOR/PURCHASER; BUYER'S REMEDIES; SPECIFIC PERFORMANCE: Defaulting seller of overencumbered property who would have received nothing on performance is not entitled to interest on purchase price in specific performance action. ***Kassir v. Zahabi, 164 CA4th 1352, 80 CR3d 1 (2008).***

In 2002, in exchange for an advance payment of six months' rent, Moe Zahabi granted his lessee, Hassan Kassir, an option to buy the leased premises for $480,000. Kassir assigned the option contract to Hassan Mannaa, with Zahabi's consent.

In July 2002, when Mannaa formally exercised the option, Zahabi refused to transfer title. Kassir and Mannaa sued for specific performance, among other things. Kassir remained in possession and paid rent into court (which rents later were transferred in trust to plaintiff's counsel) and thereafter into court again in connection with an interpleader action. In July 2004, the trial court ordered judgment for specific performance, ordering Zahabi to convey the property "free and clear of all claims, liens and encumbrances" to Mannaa for $480,000 and retaining jurisdiction for further proceedings, including the disposition of funds on deposit with the court and held in trust by counsel.

The court of appeal affirmed a money judgment, without offset, against a seller who had breached an option contract to sell residential property. The seller had failed to comply with a judgment of specific performance, declared bankruptcy, and lost his overencumbered property to foreclosure.

Zahabi refused to cooperate; the property had been overencumbered with both legitimate liens and fraudulent liens created by Zahabi. Kassir and Mannaa amended their complaint to add the lienholders. Zahabi then declared bankruptcy.

By the time Kassir and Mannaa obtained relief from the automatic stay and invalidated the fraudulent liens, the senior lienholder had foreclosed on the property, leaving no equity after satisfaction of the liens. The foreclosure occurred in 2005, and at that time Kassir apparently vacated the property and stopped paying rent.

In 2007, the trial court tried the remaining issues. The court found that, due to his exercise of the option, Mannaa became the equitable owner from the date in 2002 when Zahabi should have transferred title to him until the senior lien foreclosure in 2005. Mannaa therefore was entitled to receive the rent for that period. The amount that had been collected through the two escrows (the private attorney and the interpleader action) were not equal to that amount, and Mannaa elected to accept that amount in cash.

On appeal, Zahabi contended that the trial court lacked jurisdiction to award rents. Further, Zahabi pointed to

California precedent involving a somewhat similar case that had held that if the specific performance plaintiff is awarded rents for the period of delay in the owner's transferring the property, then the owner is entitled to an offsetting credit for the lost interest for that same period on the amount of the purchase price that would have been paid had the deal lclosed on time. and had erred in not according him an offset in the amount of the interest he would have earned on the purchase price if the sale had closed.

The court rejected the jurisdictional argument because the trial court's specific performance "judgment" was an interlocutory order. The trial court had expressly retained jurisdiction to provide further relief.

As to the offset, the court of appeal agreed that it is the general rule that when specific performance has been granted, both the seller and the buyer are entitled to receive the value of the full performance of the contract, with financial adjustments relating back to the contract date. Mannaa was entitled to a credit against the purchase price for the rents and profits from the date when title should have been transferred, and Zahabi was entitled to receive the value of his lost use of the purchase money during the period of nonperformance. Here, however, Zahabi the court ruled that Zahabi could not profit from his wrong – any award for his lost use of the purchase money could not exceed the amount of rents and profits awarded to the buyer.

The court stated that the purpose of awarding additional compensation in a specific performance action is to bring the parties as close as possible to the position they would have had if the contract had been performed. It indicated that if the escrow had closed when it should have, Zahabi still would have received nothing because the entire purchase price would have been applied to the existing liens.

Notwithstanding this, the court basically seemed to say that any discussion of an offset to Zahabi was moot, since Mannaa had elected to accept the amounts in the escrow in lieu of a judgment for the fair rental value, and the difference between those two numbers exceeded the amount of any offset to which Zahabi was entitled.

Reporter's Comment: It is difficult to know just what the court held in this opinion. Justice Sills says, in one paragraph, that the seller should receive no offset for interest because his property was fully encumbered, but then in the very next paragraph appears to uphold precisely that kind of calculation. (Although I cannot figure out why interest on $480,000 for a period of three years amounts to only $14,000.)

It is hard to see why a seller who is forced to specifically perform a sales contract, and who is held liable for the rents the purchaser would have received during the delay period, should not also get a credit for the interest on the purchase price that he would have received, whether or not his property was encumbered. Even if he was not paying his mortgages during that period, that much less of the purchase price would ultimately get to him, because the escrow officer would have to use those funds to deliver a marketable title to the purchaser – but the interest should still be included in the calculations.

Editor's Comment: The editor selected the case in order to highlight the computations that apply when specific performance is ordered, but not carried out. He hasn't seen this issue before, and the court's general analysis seems correct. He concurs with Roger Bernhardt, however, that the seller ought to be credited with the interest. In theory, of course, the seller would have had to pay interest on the senior liens encumbering the property, which he might have avoided had he received the money by performing the contract.

The Reporter for this item was Roger Bernhardt of the Golden Gate Law school, writing in the California CEB Real Property Reporter. Reprinted with permission, but edited ruthlessly without approval.

VENDOR/PURCHASER; STATUTE OF FRAUDS: The Statute of Frauds can provide a Seller with a complete defense to a contract for the sale of real estate even when the most material terms have been orally agreed upon for nearly two years but the parties have not yet reached an agreement on several less fundamental matters. ***Moorman v. Blackstock, Inc., 661 S.E.2d 404 (Va. 2008).***

In the fall of 2002, several members of a family entered into negotiations with a developer, Blackstock, to sell their old family farm. From very early on in the negotiations, the parties agreed on the most fundamental terms of a real property sale: the buyer, the seller, the property lines, and the price. However, the parties differed on some other terms, such as the timing of payment and the restrictive covenants that would be put on the land. Over the next two years, they exchanged many emails containing drafts of the contract and proposed terms, but the parties never signed a written agreement. Eventually, negotiations between the parties broke down, and the family sold the farm to another developer for a higher price in September of 2004. Blackstock sued for breach of contract of sale.

The court found for the family, indicating that, despite the existence of several broad exceptions such as equitable estoppel and part performance, the Statute of Frauds is alive and well in Virginia. Furthermore, this is exactly the type of situation that the Statute of Frauds is intended to guard against: one party claims that a contract has been formed and that he knows all of the material terms, while the other party claims that there has not yet been a meeting of the minds on all material terms. In requiring a written, signed contract for important transactions such as sales of land, the Statute makes clear for the parties (and courts) the exact moment at which a contract is formed and at which its terms become binding upon the parties.

The court supported its decision further by pointing out that the parties had exchanged written drafts of a contract but that at no point were both sides willing to sign one draft. The court saw this as evidence that the parties did not intend to form a contract orally; rather, they intended that no contract would be formed until all terms had been agreed to in writing by both sides. The court reasoned that "where parties intend to culminate their agreement with a signed contract, there is a strong presumption that no contract exists until a contract is formally signed and in writing. . . . Overcoming such a presumption requires 'strong evidence.'"

Comment 1: The case is not unique, but the fact that the case is decided by Virginia's highest court and written with the apparent intent to "deliver a message" makes if worth reporting.

It is certainly true that courts frequently find ways around the Statute of Frauds, but no thoughtful lawyer would ever count on that happening. Make the deal before you start counting the profits!!

Comment 2: What should a lawyer do when faced with a "contract that never finalizes?" Given the right circumstances, the lawyer can draft an agreement for the parties to sign that expresses the basic understandings and provides for a method of determining minor issues. Normally, however, the court will expect some "bottom line" resolution of undecided issues, so one of the parties will have to take a risk on living with that "bottom line" if other negotiations fail.

Another approach that sometimes works, when more information will make the deal easier to complete, is to turn a sale into an option, which the optionee will not exercise if the parties later fail to reach agreement on critical points, but which states some "baseline" resolutions of these points so that the optionee has something.

The editor welcomes input from others as to techniques to address these problems. But the real lesson in this case is that lawyers must make their clients aware of the need for a final, executed agreement, and to maintain momentum toward such an agreement. Hard to know whether anything would have helped in this case, but it stands as a warning to us all.

Comment 3: Note that the problem here seems to be that parts of the contract were never resolved at all – not that they simply weren't reduced to writing. Had there really been a deal, albeit unwritten, the outcome here might have been different, although the analysis would appear to be the same.

WORDS AND PHRASES; "TENANT": Tenant who had signed a lease but never received possession before landlord repudiated the lease is not a "tenant" entitled to statutory remedies available to tenants, precluding emergency of possessory action. ***Olympus Properties, LLC v. Plotzker, 888 N.E.2d 334 (Ind.App.2008),*** discussed under the heading: "Landlord/tenant; Eviction; Eviction Protection Statute; "Tenant:"

ZONING AND LAND USE; SUBDIVISIONS; EXACTIONS; OPEN SPACE: The Municipal Land Use Law gives a municipality authority to require contributions from a developer for off-tract water, sewerage, drainage, and street improvements, but does not authorize a municipality to extract monetary contributions for open space or recreational areas. ***New Jersey Shore Builders Association v. Township of Jackson, 401 N.J. Super. 152, 949 A.2d 312 (App. Div. 2008).***

ZONING AND LAND USE; PROCEDURE; AUTOMATIC APPROVAL: Even though a county planning board has only thirty days to review an applicant's plan, it can, with consent of the municipality and the applicant, have a thirty day extension, but without either consent, it must act within the initial thirty days or approval will be deemed given. ***Amerada Hess Corporation v. Burlington County Planning Board, 195 N.J. 616, 951 A.2d 970 (2008); July 16, 2008.***

The owner of a gasoline station planned to develop an adjoining property, abutting a county road. It also wanted to modify its station and build a mini mart. Since the owner's plans involved one-way egress onto the county road, it needed both municipal and county approval of the plans. The owner submitted its plans for informal review and had discussions with the county and the municipality regarding traffic and safety issues with respect to the plan. When the owner was unable to reach an agreement with the municipality or the county, it filed formal applications for site plan approval with each. After the owner submitted the additional documentation requested by the county and municipal planning boards, its applications were deemed complete.

The county planning board's engineer asked the owner's site designer for an extension of the thirty-day review period for the county to approve or reject the site plan. The county engineer claimed that it had received an extension of the review deadline, but the owner's attorney denied agreeing to an extension. Shortly thereafter, the municipal planning board approved the owner's site plan application pending the county planning board's approval of the site plan. The owner, which had not received any communication from the county board over a four-month period, filed suit asking for a declaration that the county's inaction on its site plan application triggered an automatic approval under N.J.S.A. 40:27-6.7. The lower court found that the county planning board purposefully delayed reviewing the application, and therefore it deemed the application automatically approved.

Both the Appellate Division and the New Jersey Supreme Court affirmed. The Supreme Court noted that under the Municipal Land Use Law (MLUL) and the County Planning Act (CPA), the legislature adopted strict timetables for planning board review of site plan applications. Under the statute, the county planning board has thirty days to review an applicant's plan and report back to the municipal planning board or the application will be deemed approved. The legislature recognized that the municipality has primary responsibility for site plan approval and any delays by the county in responding will bog down the process on the municipal level. The CPA allows the county planning board a single thirty-day extension with the municipality's consent, so long as the extension was approved by the applicant. The Court noted further that the MLUL addressed a problem in the predecessor statute, where inaction by a public agency was deemed a denial and agencies could deem applications incomplete, continually request information, and stall the process indefinitely. Under the MLUL, the onus is on public agencies to act quickly or the application will be deemed approved.

In this case, the county planning board argued that it mistakenly believed that it had been given an extension to respond and that it should not have been penalized. The Court, however, found that the county board could not have reasonably believed that the owner gave it an open-ended extension to approve the site plan application because it knew or should have known that the owner did not have the power to grant it. The MLUL and CPA allow only a single thirty-day extension with the municipal planning board's consent, which the county planning board never received. Therefore, it was unreasonable for it to believe it had an extension, and certainly not an open-ended one. Lastly, the Court found that the owner's attempts to reach an agreement with the county planning board after the review deadline expired did not bar the owner from seeking an order granting automatic approval.

ZONING AND LAND USE; VARIANCES: Steps toward development did not constitute reliance on zoning variance as required to timely "exercise" the variance. ***Cornell v. Board of Appeals of Dracut, 892 N.E.2d 746, (Mass.App.Ct. 2008).***

Cornell owned fourteen acres of undeveloped property that, under the city zoning by-laws of, lacked sufficient frontage for more than one lot. In March 2002, the Board of Zoning Appeals granted Cornell a variance to subdivide his parcel into two lots. Upon obtaining the variance, Cornell began to seek the necessary approvals from other town boards to subdivide and develop his property. He hired a land surveyor to finalize his two-parcel plan for presentation to the town planning board, applied to the town board of health for approval of a septic design, and sought an order of conditions from the town conservation commission. In taking these steps, Cornell spent in excess of $15,000. In June 2003, Cornell applied for a building permit, which was denied by the town building inspector on the ground that the 2002 variance had expired because it had not been exercised within one year.

In 2003, Cornell filed a complaint in land court alleging that the variance had not lapsed because his conduct – seeking approval from the planning board, board of health, and conservation commission – was sufficient to "exercise" the variance within the one year mandated by Massachusetts General Laws Chapter 40A, Section 10.

The court upheld the denial of the variance.

Massachusetts General Laws Chapter 40A, Section 10 provides clearly for a one year "exercise" requirement: "If the rights authorized by a variance are not exercised within one year of the date of grant of such variance such rights shall lapse." Whether a variance has been "exercised" is determined by the acts taken by the holder in reliance on the variance. Hogan v. Hayes, 474 N.E.2d 1158 (1985). Here, while Cornell took necessary steps toward obtaining a building permit and subdividing his land, none of his actions substantially changed his position in reliance upon the variance. Nothing prohibited Cornell from seeking these approvals simultaneously with, or even prior to, seeking the variance. Further, once he realized he would be unable to obtain the necessary permits within the year, he was free to apply for a six-month extension pursuant to Massachusetts General Laws, Chapter 40A, Section 10, yet Cornell neither recorded the variance nor sought to extend it.

Although a zoning board may, in its discretion, grant a variance, variances are not allowed as a matter of right and should be "sparingly granted." *Lussier v. Zoning Bd. of Appeals of Peabody*, 854 N.E.2d 1236 (2006), quoting from *Barron Chevrolet, Inc. v. Danvers,* 419 Mass. 404, 408, 646 N.E.2d 89 (1995).

Comment: There is probably more to the story; but, based only on the court's analysis, if Cornell had a professional handling this, there appears to be a malpractice claim. A lot of opportunities seem to have been missed.