Landlord Can’t Amend Complaint After Confessing Judgment Against Tenant

As the country continues to suffer from the recession, commercial landlords throughout Pennsylvania are being forced to deal with defaulting tenants who are thus unable to meet their financial lease obligations.

Most commercial lease agreements contain a contractual provision commonly known as a warrant of attorney which allows a commercial landlord to obtain a judgment (either for money or possession) against a defaulting tenant without providing that tenant with the opportunity to object prior to the entry of that judgment. This contractual provision is thus a quicker, easier and less costly way of obtaining judgment against a defaulting tenant than pursing claims through full-blown litigation.

A recent ruling by the Superior Court of Pennsylvania in *TCPF Limited Partnership v. Skatell*, however, illustrates why a landlord must carefully dot all of its “I’s” and cross all of its “T’s” prior to and at the time it obtains a confessed judgment.

In *Skatell*, the landlord agreed to lease a portion of a building to a tenant for the operation of a sandwich shop for a period of seven years. Since the tenant was incorporated, the landlord required the tenant’s president and others to separately agree to guarantee the tenant’s monetary obligations under the lease, according to the opinion. The guaranty agreement contained a warrant of attorney enabling the landlord to bring an action to confess judgment against the guarantors for any and all amounts due under the lease. The guaranty agreement contained language allowing for the

successive exercises of the warrant of attorney until all monetary obligations under the lease had been discharged.

When the tenant committed monetary breaches under the lease, the landlord filed a complaint in confession of judgment against the guarantors of the lease seeking approximately $60,000, the opinion said. In the complaint, the landlord invoked the right to accelerate the rent and other charges due for the balance of the lease term. On the same day the complaint was filed, judgments by confession were entered in favor of the landlord and against the guarantors.

Subsequent to the filing of the complaint and entry of the confessed judgments, the landlord discovered that it had miscalculated the amount due under the lease by almost $150,000, the opinion said.

The landlord then requested leave of court to file an amended complaint in confession of judgment to increase the judgment amount to account for the amount which was actually due for the balance of the lease term. The trial court denied the landlord’s request.

The landlord then presented a second motion for leave to file an amended complaint. In that motion, the landlord sought to amend the paragraph of the original complaint where the landlord invoked its right to accelerate the balance due under the lease. Under the proposed amendment to the original complaint, that paragraph stated that the landlord would only be seeking that part which the landlord had already obtained judgment for, thus reserving the right to confess judgment for other amounts coming due under the lease. The trial court denied that motion as well.

The landlord then appealed the denial of both of these motions to the Superior Court.

The Superior Court first addressed the trial court’s refusal to allow the landlord to file the first amended complaint.

The landlord argued that it had the right under Rule 1033 of the Pennsylvania Rules of Civil Procedure to amend the original complaint to take into account the amount which was actually due under the lease.

Rule 1033 provides that a party to litigation may, either by filed consent of the adverse party or by leave of court, amend a complaint. The landlord contended that, since Rule 1033 allows for liberal amendments and because the proposed amendment did not "'present an entirely new cause of action or unfairly surprise or prejudice an opposing party' the amendment should have been granted by the trial court."

The Superior Court, however, reinforced that an amendment is not permitted under Rule 1033 "where it is against a positive rule of law".

According to the Superior Court, the trial court correctly ruled that the landlord was clearly "'without authority' to reflect a different calculation of damages for the entire unexpired term of the lease" in that, "under the law of Pennsylvania, a warrant of attorney to confess judgment may not be exercised twice for the same debt." In other words, where a power of attorney authorizes a confession of judgment and the power is once exercised, the power is thereby exhausted.

The Superior Court noted that, in the original complaint, the landlord had already invoked its right to accelerate the amount due under the lease for the balance of the lease term and sought and obtained judgment of a specified amount. By doing so, the Superior Court believed that the landlord's power under the warrant of attorney was thus exhausted for the monetary breaches which had been committed by the tenant under the lease.

The Superior Court also agreed that the trial court properly denied the second attempt by the landlord to amend the

original complaint because the landlord was, in essence, attempting to exercise the warrant of attorney twice for the same debt. ¨The landlord argued that the second attempt to amend the original complaint was legally permissible because the proposed amendment did not seek to alter the amount of judgment and, thus, did not require the exercise of the warrant of attorney. Rather, according to the landlord, the proposed amendment sought to correct a paragraph in the original complaint to state that the landlord was merely invoking its right to accelerate a portion (not all) of the amount due under the lease. In doing so, the landlord emphasized that the proposed amendment would require no new judgment, would keep the original confession of judgment intact and would allow it to confess another judgment for the remainder of the lease term.

The Superior Court found that the landlord was prohibited under Rule 2953 of the Pennsylvania Rules of Civil Procedure from so amending the original complaint.

Under Rule 2953, "[w]here an instrument authorizes judgments to be confessed from time to time for separate sums as or after they become due, successive actions may be commenced and judgments entered for such sums."

The Superior Court pointed out that Rule 2953 restricts successive actions to "separate sums" claimed due and collectible under a warrant of attorney as contrasted to the "same sum" of money already confessed.

As for the second proposed amendment, the Superior Court believed that, since judgment had already been entered to collect the balance of the lease term, the landlord could not amend the original complaint so as to reserve the right to a subsequent exercise of the warrant of attorney for a separate sum because the warrant of attorney had already been exhausted for the underlying monetary breaches.

LESSONS LEARNED

A landlord only gets one bite of the proverbial apple to confess judgment. That is not to say that the landlord cannot ever seek what is due and owing under the lease in a situation like *Skatell*. Rather, the landlord cannot confess judgment and must rather stand in line for his day in court with the other plaintiffs.

Alan Nochumson

Vertical Position 100%

Attempted Oral Modification Of Written Agreement Of Sale Disallowed

Whether the purchase involves residential or commercial real estate, the mindset should be the same, buyer beware. Because most real estate transactions are entered into at arms-length, it is important for potential purchasers to condition the sale on what they believe the property "is" so they can be allowed out of the transaction if the property turns out differently during the due diligence stage of the transaction. This is especially true when purchasing commercial real estate. The property is more than the physical structure. The value of

the property also depends upon the revenue stream generated presently and potentially in the future from the property.

A recent decision handed down by the U.S. District Court for the Eastern District of Pennsylvania in *The Herrick Group & Associates LLC v. K.J.T., L.P.* only reinforces why it is so critical for potential purchasers to include language in their agreements of sale permitting them to remove themselves from the transaction prior to closing without penalty if the property does not turn out the way it was represented to them.

In *K.J.T., L.P.*, KJT owned a property located in Reading, Pennsylvania known as Washington Towers which consists of commercial space and residential apartment units, as noted in the opinion. The commercial space was being leased by a grocery store and technology company which had separate leases running concurrently.

KJT eventually entered into an agreement of sale for the building with The Herrick Group, a company which often bought and sold commercial real estate for “flip transactions”, the opinion said.

In the agreement of sale, KJT represented and certified as true both at the time of the execution of the agreement of sale itself and through closing that each tenant in the building had the right to occupy space in the building pursuant to a written lease, that all leases were full force and effect, and that it had no knowledge of any breach of any lease, as noted in the opinion.

Moreover, KJT was responsible for delivering so-called “estoppel letters” just prior to closing to Herrick which confirmed, among other things, that the leases were unmodified (or state the modification) and in full force and effect, the dates to which rent and other charges have been paid, and state that KJT is not in default of any of the leases, as noted in the purchase and sale agreement references in the

opinion.

If Herrick was unsatisfied with the content of any of the "estoppel letters", it had to make an objection within a prescribed period of time or it would waive any such issue with the "estoppel letters".

Under the agreement of sale, if KJT failed to so deliver the "estoppel letters", Herrick had the option to proceed forward with the closing or terminate the agreement altogether with KJT allowing the security deposit to be returned to Herrick along with accrued interest.

The parties also stipulated in the agreement of sale itself that it could only be amended by a written memorandum subsequently executed by the parties.

After the agreement was executed, Herrick performed due diligence of the property. Closing of the property was extended twice by mutual agreement of the parties and in writing, once in return for the payment of an additional deposit and the other times without charge.

Apart from the extensions of the closing date, the parties also entered into a letter agreement making additional changes to the agreement. Among other things, Herrick was allowed to assign its rights under the agreement to an unrelated third party, which it eventually did, as noted in the opinion.

Soon after the agreement was signed, an estoppel letter was obtained for the grocery store which stated that rent was paid in full even though that was incorrect. After the estoppel letter was executed but prior to the closing date, the grocery store abandoned its leased premises and ended its tenancy prematurely.

The estoppel letter issued with regards to the technology company faired no better. That letter did not reveal that the technology company had already abandoned its leasehold and

that it owed gas, water, and parking fees under the lease agreement, the opinion said.

KJT eventually discovered that the grocery store abandoned the leased premises prior to the closing date (but did not discover the issues involving the technology company until after KJT commenced litigation against Herrick), the opinion said.

After discovering the abandonment of the leased premises by the grocery store, the parties engaged in negotiations to salvage the sale. The bank financing the deal was also involved in these negotiations. During the negotiations, there were discussions about one of KJT's principals offering to guarantee the rental payments due under the grocery store lease. These discussions took place verbally and in writing and focused on whether the guarantee would be for the term of the lease or a part thereof and if the amount otherwise due would be placed in escrow at the time of closing as demanded by the bank.

Although no formal agreement was ever entered into between the parties as to the "rent guarantee" and signed by them, KJT claimed such an agreement had been orally reached by the parties. Herrick disputed that a deal had been struck with respect to the "rent guarantee" and, due to the impasse, declared its intention to terminate the agreement. Herrick then demanded that KJT allow the deposit made on account of the agreement be returned by Herrick. When KJT refused, Herrick filed suit in federal district court seeking the return of the deposit.

The federal district court in *K.J.T., L.P.* ruled that the deposit should be returned to Herrick because of the material breaches of the agreement committed by KJT and the failure of the parties to resolve these breaches through a modification of the agreement.

The federal district court's ruling hinged on whether the parties had entered into a modification of the agreement which cured the breaches of the agreement through the "rent guarantee" allegedly promised by one of KJT's principals.

In Pennsylvania, "[a]n agreement that prohibits non-written modification may be modified by subsequent oral agreement if the parties' conduct clearly shows the intent to waive the requirement that the amendments be made in writing. An oral contract modifying a prior written contract, however, must be proved by clear, precise and convincing evidence."

The federal district court believed "although it [wa]s a close question whether KJT secured from Herrick a binding oral modification to guarantee the lease payments, KJT's evidence of the modification f[ell] short of the 'clear, precise, and convincing evidence' required to prove such amendments."

In doing so, the federal district court noted that, while "KJT may have subjectively believed it had addressed Herrick's concerns on the eve of closing, . . . relevant correspondence among the parties establishes the topic of lease guarantees remained a disputed issue until negotiations ended" and that "KJT failed to avail itself of ample opportunities to obtain a written amendment", unlike the other modifications to the agreement which had been memorialized in writing.

LESSONS LEARNED

The underlying facts and circumstances in *K.J.T., L.P.* clearly shows why it is vital for potential purchasers not to permit themselves to be trapped into an undesirable situation. Through good draftsmanship, KJT was forced to make certain representations about the tenants in the building. When these representations proved to be false, Herrick was allowed to terminate the deal.

Additionally, what saved Herrick from a financial disaster was the prohibition regarding oral modifications. While the

federal district court found it to be a “close question”, that provision in the agreement prevented KJT from claiming verbal discussions and innuendos formed the basis of an agreement binding the parties in contract. Without that provision in place, the federal district court may well have found that Herrick forfeited its deposit.

Alan Nochumson

Vertical Position 100%

Nochumson Teaches About Drafting Lease Agreements

Alan Nochumson served as a faculty speaker at a Continuing Legal Education (CLE) seminar entitled *Landlord & Tenant Law in Pennsylvania – Beyond the Basics In the New Economy* which was sponsored by Sterling Education Services, Inc.

During the seminar, Nochumson explained what terms and conditions should be in every lease agreement in Pennsylvania from both a landlord and tenant perspective.

Vertical Position 35%

Attorney’s Fee Provision In Residential Lease Enforced Against Defaulting Tenant

In Pennsylvania, parties to litigation are responsible for their own legal fees and costs unless they otherwise contractually agree that the prevailing party will be reimbursed for such fees and costs at the conclusion of litigation.

In a decision handed down earlier this year in *Bayne v. Smith*, the Superior Court of Pennsylvania recently allowed a landlord to collect attorney’s fees from a defaulting tenant in accordance with the terms of a lease agreement entered into by the parties.

In *Bayne*, the landlord and tenant entered into a written month-to-month residential lease. When the tenant failed to pay rent and caused damage to the leased premises, the landlord instituted an action against the tenant before the local Magisterial District Justice. Following a judgment in favor of the landlord and against the tenant, the tenant filed an appeal for a trial *de novo* before the Court of Common Pleas.

The trial court entered an order upon the consent of the parties, finding judgment in favor of the landlord and against tenant in the amount of $410.14 due to the admitted breaches of the lease. This amount represented property damages and partial rent less the security deposit of $175.00 previously paid by the tenant. Additionally, the order directed that the entry of judgment would be stayed pending a determination by the trial court on the landlord’s request, pursuant to the terms of the lease, for inclusion of attorney’s fees as part of the judgment amount.

The trial court eventually denied the landlord's request for the inclusion of attorney's fees as part of the judgment amount. In reaching its conclusion, the trial court pointed out that residential leases are seldom the resulting of any negotiating between the parties and the tenant generally lacks any bargaining power and must thus accept the landlord's terms "as is".

The landlord in Bayne then appealed the trial court's denial of the reimbursement of attorney's fees to the Superior Court.

The Superior Court ultimately concluded that the trial court erred in refusing to permit the recovery of attorney's fees.

The general rule in Pennsylvania is that "there is no recovery of attorney's fees from an adverse party in the absence of an express statutory authorization, clear agreement between the parties, or the application of a clear exception." That rule of law is no different with respect to the landlord-tenant relationship. As acknowledged by the Superior Court, while the Landlord and Tenant Act of 1951 does not specifically provide for the recovery of attorney's fees, it does not prohibit the inclusion of a fee-shifting provision in rental agreements. The Superior Court instead emphasized that the validity of such a provision is solely dependent upon contract law. As such, the Superior Court provided that "[w]here the language of a lease is clear and unequivocal, its meaning will be determined by its contents alone in ascertaining the intent of the parties."

Although conceding that the lease included an attorney's fees provision, the tenant argued that the lease was an adhesion contract and that the provision was unconscionable and thus unenforceable.

The Superior Court sidestepped whether the lease was an adhesion contract and stated that, even if the lease was categorized as one of adhesion (which it did not), the "terms

must be analyzed to determine whether the contract as a whole, or specific provisions of it are unconscionable."

Instead of addressing whether the tenant lacked a meaningful choice about whether to accept the fee-shifting provision, the Superior Court simply noted that the lease was a simple two-page document containing an attorney's fee provision which is not typically found in every rental agreement. The Superior Court did not believe that the provision unreasonably favored to the drafter of the lease (i.e., the landlord) as it allowed for the recovery of attorney's fees to the prevailing party. As noted by the Superior Court, as a result of the provision's neutrality in application, if the tenant had successfully defended the landlord's claims, the tenant would have been entitled to recover her attorney's fees under the fee-shifting provision.

LESSON LEARNED

The factual circumstances of *Bayne* only reinforces why landlords across the commonwealth should strongly consider including a contractual provision in lease agreements obligating their tenants to reimburse them for the legal fees and costs they expend in the event of breach.

In *Bayne*, the tenant only owed $410.14 to the landlord as a result of breaches committed under the lease. The landlord in seeking enforcement of the lease expended legal fees and costs which most definitely exceeded the amount in controversy.

Similarly, without a fee-shifting provision, landlords, if forced to retain the services of an attorney to collect the amount of money owed, may very well eat into their respective anticipated profit or, worse, the cost of doing business.

When a tenant commits a default under a lease agreement, all the landlord wants is to be made whole as if the breach never occurred. That is impossible if the landlord must also pay an attorney to get the amount owed under the lease agreement.

By including a contractual provision which shifts the costs of litigation, a landlord may very well avoid litigation altogether. Many landlords face situations where a defaulting tenant makes a low settlement offer figuring that the costs associated with litigation and the delays inherent in the judicial process will deter the landlord from filing suit. A contractual provision that potentially shifts the costs of litigation to the defaulting tenant will make such underhanded tactics ineffective.

For all of these reasons, there is no reason why a landlord should not include an attorney's fee provision in a lease agreement.

Alan Nochumson

Vertical Position 100%

Court: City's Liability Limited On Sidewalk "Slip And Falls"

The common law has traditionally imposed on property owners the duty to maintain the sidewalks abutting their properties. However, pedestrians should be wary of a gap in coverage created by the Pennsylvania legislature that could leave an

injured pedestrian with no liable party to recover from if the injury occurred on a sidewalk that is adjacent to a street owned by a governmental entity.

In *Reid v. City of Philadelphia*, the Pennsylvania Supreme Court recently overruled the Commonwealth Court of Pennsylvania's decision in *Sherman v. City of Philadelphia* that "rewrote" an exception to governmental immunity which imposes liability for torts arising out of the care, custody or control of real property to include sidewalks that adjoin real property owned by the municipality.

In *Reid*, the plaintiff filed a negligence action against the City of Philadelphia after injuring his ankle when he slipped and fell on a sidewalk outside Philadelphia's 39th District Police Station. The plaintiff in *Reid* alleged that he fell because of the City's failure to remove ice and snow from the sidewalk.

The City raised the affirmative defense of governmental immunity pursuant to the Political Subdivision and Tort Claims Act, or the Act. The Act provides for governmental liability arising from the care, custody or control of real property possessed by a governmental entity.

Using this exception, the trial court found the City was primarily liable for the plaintiff's injuries due to its negligence in failing to remove the ice and snow from the sidewalk, a dangerous situation that was exacerbated by allowing their employees to park their vehicles on the sidewalk.

On appeal, the Commonwealth Court affirmed the trial court's ruling basing upon the rationale set forth in *Sherman v. City of Philadelphia*, wherein the Commonwealth Court previously held that "where a municipality is the owner of real property that adjoins a sidewalk, the municipality can be held primarily liable . . . as property owner for its failure to

satisfy its obligations to make sidewalks safe for pedestrian travel."

The Commonwealth Court also cited to a Supreme Court decision in *Walker v. Elby*, as having "tacitly" accepted the *Sherman* decision. In *Walker*, the Supreme Court concluded that, "for purposes of the sidewalks exception clause, a state highway running through local agency property is considered a local-agency-owned street," and therefore "any injuries occurring on a sidewalk adjacent to a state-designated highway fell within the 'right of way of a street owned by the local agency'" so therefore the sidewalk exception clause to government immunity would apply.

In *Reid*, however, the Supreme Court agreed with the argument made by the City that the real property exception does not apply to sidewalks and should be distinguished from the separate sidewalk exception clause also contained in the Act. The Act specifically states in the real property exclusion clause that sidewalks are not to be included in the definition of "real property."

Moreover, the sidewalk exception clause in the Act imposes a higher burden of proof than the real property clause by additionally requiring that "the dangerous condition created a reasonably foreseeable risk of the kind of injury which was incurred and that the local agency had actual notice or could reasonably be charged with notice under the circumstances of the dangerous condition at a sufficient time prior to the event to have taken measures to protect against the dangerous condition." The sidewalk exception clause in the Act also only imposes secondary liability where "such other person shall be primarily liable."

The Supreme Court determined that "[a] plain reading of [the real property exception clause] reveals the legislatures intended the clause establishing the real property exception be inapplicable to injuries arising from sidewalks, even if

the sidewalk abuts" governmentally owned property.

Revisiting *Sherman*, the Supreme Court said "We disagree with *Sherman* to the extent it expanded [the real property exception clause] definition of real property to include sidewalks that abut public property."

The Supreme Court looked to the dissenting opinions in *Sherma*n and agreed that the *Sherman* majority "improperly rewrote the Act under the pretext of reaching a desired result." Specifically, the *Sherman* majority had determined that the "General Assembly, when drafting the exceptions to governmental immunity, did not envision nor consider the situation where the local agency owns the property adjacent to the sidewalk on which the injury occurs and the Commonwealth owns the street abutting that sidewalk" and therefore there was a "gap in coverage" under the Act resulting in no party being held liable for those injuries occurring on an agency maintained sidewalk that is adjacent to a state highway.

The Supreme Court, however, refused to allow the gap to be closed by the *Sherman* decision. Partially quoting one of the *Sherman* dissenters, the Supreme Court stated that "[e]ven if the legislature failed to contemplate the situation where the local agency owns the property adjacent to the sidewalk, it does not follow that the solution is for this [C]ourt to engraft language onto the legislature's definition of real property where the engrafted language runs directly contrary to the express words. Rather, the solution is to give full effect to the clear and unambiguous language . . . and urge the legislature to resolve the problem by enacting proper amendments to the statute."

In support of its ruling, the Supreme Court explained that "[i]t is only when the statute's words are not explicit that the legislature's intent may be ascertained" and "[w]hen the words of a statute are clear and free from all ambiguity, they are presumed to be the best indication of legislative intent."

The Supreme Court also rejected the plaintiff's alternative argument which was further geared towards access to the real property exception: that "the City transformed the sidewalk into a parking lot because it regularly allowed its employees to park vehicles on the sidewalk." While parking lots are not excluded under the real property exception, the Supreme Court believed that the plaintiff was unable to support the contention that a sidewalk could be transformed into a parking lot "merely by parking an indeterminate number of vehicles on it."

LESSONS LEARNED

Until the time comes when the legislature sees fit to address this oversight of this idiosyncratic situation, governmental immunity will shield governmental entities from legal liability under similar circumstances. Pedestrians throughout the City should thus be mindful of this while walking on sidewalks on properties governmentally owned and maintained.

Alan Nochumson

Vertical Position 100%

Nochumson P.C. Protects

Property Owner From Tax Foreclosure

In a case of first impression, Nochumson P.C. convinced the Commonwealth Court of Pennsylvania in *City of Philadelphia v. Schaffer* to limit the City's ability to expose properties to sheriff's sale due to a property owner's failure to pay real estate taxes.

While the property owner in *Schaffer* was delinquent in her real estate tax payments, the Commonwealth Court nevertheless agreed to invalidate the sale because the City failed to comply with the procedural requirements mandated under state law.

The Commonwealth Court's decision will greatly impact the way the City conducts its business in the prosecution of tax delinquencies.

For a copy of the court opinion, please feel free to contact us.

Vertical Position 8%

Mortgage Lender, Broker Absolved For Loan Irregularities

Nowadays, there is at least one newspaper or television account of how the residential mortgage crisis was caused by the shaky underwriting practices previously employed by our

financial institutions.

In a recent decision handed down in *Morilus v. Countrywide Home Loans, Inc.*, the U.S. District Court for the Eastern District of Pennsylvania recently dealt with such a convoluted transaction.

THE CASE

In early 2005, a married couple attempted to purchase a house for themselves. Their poor credit, however, prevented them from receiving favorable mortgage terms, according to the opinion. As a result, their mortgage broker suggested that the couple find someone else they know to obtain a mortgage on their behalf and for the couple then to make the monthly payments due under the mortgage as though the couple owned the house themselves (even though they would not).

The couple eventually convinced a friend to purchase the house for them by placing the mortgage in the friend's name, the opinion said. Although the husband and wife were not signatories to the mortgage, it was understood by their mortgage broker and friend that the couple would reside at the house and make the friend's mortgage payments, the opinion said. Only a year after the closing, the friend was forced to sell the house because of the married couple's inability to make the mortgage payments, according to the opinion.

The married couple and their friend then instituted suit against the mortgage broker and mortgage lender on the theory that they "conspired to unfairly and deceptively induce [them] to execute loan documents . . . to qualify them for a loan with monthly payments they could not afford."

In the complaint, the married couple and their friend alleged that the mortgage broker and mortgage lender misrepresented the friend's assets and inflated the price of the house, requiring the married couple, in essence, to enter into a second mortgage to purchase the house.

THE DECISION

The district court first addressed whether the married couple even had standing to bring suit. The mortgage lender argued that the "legal interests created with the mortgage belong to the signing parties," and because the married couple were not signatories to the mortgage, they failed to raise their own rights. The district court agreed with the married couple that they had standing because the only reason they did not sign the mortgage was as a result of the mortgage lender and mortgage broker intentionally keeping them off the mortgage, which, if proven at trial, would violate Pennsylvania's Unfair Trade Practices and Consumer Protection Law, or UTPCPL.

The district court next determined whether the lender was liable for the actions of their mortgage broker under an agency theory. The elements of an agency relationship are "the manifestation by the principal that the agent shall act for him, the agent's acceptance of the undertaking and the understanding of the parties that the principal is to be in control of the undertaking."

The mortgage lender argued that there was no evidence of a manifestation of intent for the mortgage broker to act on its behalf nor was there ever an understanding between itself and the broker.

In response, the married couple and their friend stated that the mortgage lender had exerted such a high level of control such that the mortgage broker must be an agent (and not an independent contractor).

The district court concluded that to be deemed an agent, the control "must be of such a high degree that the purported agent is deemed to have had almost no independence." In contrast, the district court believed that the married couple and their friend could only show that, should the mortgage broker conduct business with the mortgage lender, then the

broker was required to abide by certain guidelines set forth by the lender.

The district court then rejected the claim of apparent agency. The theory of apparent agency rests upon whether a principal "leads persons with whom his agent deals to believe he has granted certain authority which actually exceeds the scope of the agency."

The district court reasoned that the married couple and their friend were unable to show evidence of an action by the mortgage lender which would indicate that the mortgage broker was its apparent agent. In particular, the district court pointed out that the mortgage broker had the ability to submit the mortgage application to any mortgage lender in the industry, not just the ultimately selected mortgage lender.

The district court next addressed the Real Estate Settlement Procedures Act, or RESPA, claim contained in the complaint. RESPA was designed to "ensure that consumers are made aware of settlement procedures and costs by imposing certain disclosure requirements, and to eliminate kickbacks and referral fees which increase the cost of the settlement process."

In the complaint, the married couple and their friend alleged that the mortgage lender engaged in kickbacks in the form of an undisclosed property appraisal charge. The district court dismissed the claim as barred by the statute of limitations since they were required to file the claim within one year of the alleged violation which, in this case, was the date of the closing (which they did not).

The district court next examined the UTPCPL claim. A cause of action under the UTPCPL only exists if the plaintiff can show that he "justifiably relied on the defendant's wrongful conduct or misrepresentation and that he suffered harm as a result of that reliance."

The district court rejected the contention of the married

couple and their friend that the mortgage lender induced them to act to their detriment. The district court reiterated that the mortgage broker was not the mortgage lender's agent, and thus, without an agency relationship, the married couple and their friend had no grounds to justifiably rely upon any representation because they had not had any interaction with the mortgage lender. In short, the district court believed "[w]ithout a representation, there was no misrepresentation."

The district court then addressed the mortgage lender's attempt to move for summary judgment on its fraud and conspiracy claims against the married couple and their friend. Under the mortgage, the house was required to be the primary residence of the signatory, the married couple's friend. The mortgage lender alleged that the friend had committed fraud by signing the mortgage with no intention of making the house her primary residence nor was it ever her primary residence.

Because there was no evidence to establish that the mortgage lender knew of the arrangement made by the married couple with their friend, the district court found that the mortgage lender was justified in relying upon the representation made in the mortgage.

Moreover, the district court recognized that the mortgage lender had indeed suffered damages as a result of the fraudulent conduct perpetuated by the married couple and their friend, reasoning that a higher interest rate would have been charged had the mortgage lender known that the married couple, not the friend obtaining the mortgage loan, would be residing in the house.

The district court, however, refused to grant summary judgment in the mortgage lender's favor with respect to its conspiracy claim against the married couple and their friend.

Civil conspiracy requires proof that "a combination of two or more persons act[ed] with a common purpose to do an unlawful

act or to do a lawful act by unlawful means or for an unlawful purpose," and an overt act done to pursue this common purpose that results in actual legal damage. Furthermore, the plaintiff must prove malice or the intent to injure.

The district court held that the married couple and their friend were acting to advance the married couple's interest in home ownership, and not with malice or the desire to cause the mortgage lender any harm.

LESSONS LEARNED

As the housing crisis has shown, the factual circumstances of cases like *Morilus* are, sadly, not that uncommon. For the past decade, some mortgage brokers would say and do whatever was necessary to close the "deal", even if it was to their client's detriment.

The district court in *Morilus* refused to allow the married couple and their friend to shift the blame onto the mortgage broker and mortgage lender. Instead, the district court, through its ruling, essentially stated that they "made their bed, know they have to lie in it" because, even if the contours of the mortgage arrangement were originally suggested by the mortgage broker, they made the ultimate decision to proceed forward.

With more and more individuals losing their jobs, and given the depressed real estate market, *Morilus* is just the first round of this type of litigation. The victor today is the mortgage industry.

Alan Nochumson

Vertical Position 100%

Nochumson Speaks About The Eviction Process In Pennsylvania

Alan Nochumson spoke about the eviction process in Pennsylvania as a faculty speaker at a Continuing Legal Education (CLE) seminar entitled *Landlord-Tenant Law Update* which was sponsored by Sterling Education Services, Inc.

Vertical Position 34%

Developer Cannot Sue In Federal Court To Challenge State Court Judgment

In *Flannery v. Mid Penn Bank*, the U.S. District Court for the Middle District of Pennsylvania recently rejected a judgment debtor's attempt to essentially challenge, in federal court, the validity of a state court judgment obtained against him related to a failed real estate development venture.

In 2004, four individuals formed a real estate development company to own commercial real estate in Harrisburg, Pennsylvania. Each of the individuals had a 25% ownership

interest in the company. The plaintiff in *Flannery* subsequently purchased the full interest of one of the original members and half of the interest of another member.

The company performing the construction work on the property was owned and operated by one of the members of the real estate development company, the opinion noted.

The following year, Mid Penn Bank extended a $500,000 loan to a prospective tenant. The bank extended the loan so the prospective tenant could pay the general contractor for the construction work being performed on the commercial property. The real estate development company, the plaintiff and his wife and the remaining two members of the real estate development company, among others, personally guaranteed the loan.

When the tenant eventually defaulted under the loan, the bank sought judgment by confession against the tenant, the plaintiff and his wife, and the other members of the real estate development company, among others, the opinion noted.

Afterwards, the bank not only agreed to release one of the other members of the real estate development company as a personal guarantor under the loan but to also assign its interest in all of the judgments obtained by the bank to that member. According the plaintiff, the bank agreed to so because the member had substantial business and personal investments with the bank.

Rather than attempt to strike or open the confessed judgment entered against him by the bank which was now in the possession of the member who had obtained that judgment from the bank, the plaintiff instead decided to sell his interest in the real estate development company to that member in order to satisfy the judgment levied against him.

The plaintiff then filed a complaint in federal district court

against the bank and some of its officers.

The complaint was fundamentally based upon the theory that the bank and its officers colluded with that member to defraud the plaintiff out of his interest in the real estate development company.

The defendant then filed a motion to dismiss the complaint which was based primarily upon the grounds that the Rooker-Feldman doctrine barred all of the claims contained in the complaint.

Under the Rooker-Feldman Doctrine, "federal district courts lack subject matter jurisdiction over challenges that are the functional equivalent of an appeal of a state court judgment . . . even if those challenges allege that the state court's action was unconstitutional."

A claim is determined to be the "functional equivalent of an appeal" if that claim is either a claim that was actually litigated in state court or if the claim is "inextricably intertwined" with the state court adjudication.

According to the federal district court in *Flannery*, the promissory note signed by all the loan guarantors contained a confession of judgment clause, which "permits the creditor or its attorney simply to apply to the court for judgment against the debtor in default without requiring or permitting the debtor or guarantors to respond at that juncture."

As noted by the federal district court, after a confessed judgment is obtained, the defendant may petition the court to strike or open the judgment.

Because the plaintiff did not petition the state court to strike or open the confessed judgment obtained against him, the federal district court concluded that there was no adversarial proceeding in which the merits of any defenses were adjudicated and, therefore, the claims contained in the

complaint were not actually litigated.

After determining that the claims contained in the complaint were not actually litigated in state court, the federal district court next addressed whether the claims were "inextricably intertwined" with the state court proceedings.

The federal district court reasoned that, if it had to decide that the state court was wrong, or if it had to act in a way that would make the state court's judgment ineffectual, then the claims contained in the complaint would be considered "inextricably intertwined."

The federal district court ultimately found its lack of jurisdiction over the claims contained in the complaint because "[f]or the court to find that [d]efendants procured the guaranty by fraud would necessarily imply that the state court erroneously entered the confession of judgment."

LESSONS LEARNED

The federal district court's ruling in *Flannery* illustrates why litigants must exhaust all of their legal and equitable rights and remedies in state court rather than perform the proverbial "end-run-around" in federal court.

In *Flannery*, the plaintiff could, and now knows should, have challenged the validity of the confessed judgment obtained against him in state court. Rather than doing so, he allowed his business partner, who had purchased the bank's interest in that judgment, to, in his mind, steal the real estate development company out from under him.

Noticeably absent from the federal court proceedings is the inclusion of the former business partner as a party defendant. The plaintiff likely did not sue him either because he already waived any claims he had or would have had against him when he agreed to sell his interest in the company to him in exchange for the satisfaction of the judgment by confession or the

plaintiff knew that the applicability of the Rooker-Feldman Doctrine would only be strengthened if he included him as a party defendant. Either way, the federal district court, through its ruling, merely reinforces why the plaintiff should have litigated his claims against the former business partner, the bank, and others within the state court proceedings.

Alan Nochumson

Vertical Position 100%

Association Can't 'Selectively Prosecute' Property Rights

What happens when your neighbor accidently builds a physical structure onto land which adversely affects your property interest to access that land? That question was partially answered in *Big Bass Lake Community v. Warren* where the Commonwealth Court of Pennsylvania held that the trial court had improperly granted an injunction to a homeowner's association in a planned community.

In order to give themselves more privacy, several lot owners in the planned community built ground planters supported by a short stone wall that bordered their property lines. Most of

the wall ran adjacent to a road owned by the homeowner association to which all lot owners had access. The wall was placed approximately three feet from the edge of the paved portion of the road.

Several days after beginning construction, an employee of the homeowner association advised one of the lot owners that the wall would interfere with its right to install utility fixtures and lines which is contained as a restrictive covenant in each of the deeds held by lot owners in the planned community, the opinion noted.

After the lot owners refused to remove their wall, the homeowner association filed a complaint claiming that no improvements were allowed within the utility easement and that the improvements were within its right-of-way which abutted the lot owners' property, according to the opinion.

The homeowner association then filed a petition for a preliminary injunction, the opinion noted.

Although the homeowner association conceded that other lot owners had encroached upon its right-of-way with landscaping improvements and stone walls in the past, it did not believe those encroachments were as significant given that the stone walls in dispute were further within the boundary of the easement, the opinion noted.

The homeowner association further claimed that the installed walls would make plowing of the road difficult due to the inability to push the snow over the walls. In comparison, the homeowner association explained that the other walls and landscaping features installed by other lot owners in the planned community were not as serious an impediment to snow plowing, according to the opinion.

Regardless, the homeowner association pointed out that it was now pursuing enforcement for the unrelated encroachments as well, the opinion noted.

The lot owners, while admitting that the homeowner association has a right to go onto their respective properties to place a utility line or fixture, are not prevented by the restrictive covenant which runs with the land from making improvements in that portion of the properties controlled by the easement and they otherwise are not required to obtain prior approval from the homeowner association before doing so. They also denied that the stone walls impeded snow removal based upon experience from a previous snowstorm.

The trial court issued an injunction after finding that the stone walls were indeed an encroachment and that the construction of the walls violated the restrictive covenant contained within the deeds, according to the opinion.

The lot owners then appealed the trial court's ruling to the Commonwealth Court.

The Commonwealth Court first addressed whether the homeowner association even had a clear right to the injunction due to its failure to pursue immediate legal recourse against the lot owners who similarly landscaped.

The Commonwealth Court notes that an injunction "is an extraordinary remedy that should be issued with caution and 'only where the rights and equity of the plaintiff are clear and free from doubt, and where the harm to be remedied is great and irreparable."

However, the Commonwealth Court did clarify that even a very insignificant encroachment can be ordered to be removed by injunction as "occupation of an adjoining land owner's property, if continued, 'will ripen into a complete title'" and the land will be lost to your neighbor forever.

The Commonwealth Court disagreed with the homeowner association's belief that the lot owners could not landscape at all within the land devoted to the utility easement.

Even if there is proof of an encroachment, its mere existence does not necessarily guarantee injunctive relief. Citing to the Supreme Court of Pennsylvania's decision in *Moyerman v. Glanzberg*, the Commonwealth Court discussed the equitable considerations in deciding whether an injunction is appropriate.

In *Moyerman*, the Supreme Court found that because the defendant had substantially completed his project before realizing he was building 16 inches onto his neighbor's property and the encroachment did not "materially interfere" with the plaintiff's use of his driveway that the "equities did not favor an injunction."

The Supreme Court, however, cautioned that equities will not matter when "a defendant has deliberately and willfully built upon plaintiff's property, tortiously or in bad faith, injunctive relief should be granted, regardless of the equities."

The Commonwealth Court said that "[i]f the easement forbade improvement in the utility easement area, then a lot owner's grass lawn would have to terminate ten feet shy of each of the four sides of a lot. This is illogical and unnecessary. When the Association finds it necessary to exercise its right under the utility easement, the Association can remove whatever grass, bush or flower bed has been planted in the easement area."

The Commonwealth Court found that the encroachment was not a significant interference with the use of the right-of-way and that, since building the wall was not performed tortiously or in bad faith, no injunction was merited.

Furthermore, the Commonwealth Court concluded that the equities did not favor the homeowner association because of its longstanding tolerance of similar landscaping projects.

LESSONS LEARNED

The Commonwealth Court's ruling in *Big Bass Lake Community* shows why property interests should be vigorously protected. In *Big Bass Lake Community,* the Commonwealth Court was swayed by the homeowner association's failure to seek legal recourse against lot owners who had made similar encroachments. The Commonwealth Court basically found that the homeowner association could not selectively prosecute its property rights.

Another lesson learned from *Big Bass Lake Community* is the importance of defining property in the chain of title. Easements are generally disfavored by the courts. With that in mind, the Commonwealth Court restrictively read the language in the deeds granting the homeowner association a right of way over the lot owners' respective properties.

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Vertical Position 100%