

NEWSLETTER OF THE REAL PROPERTY SECTION OF THE MISSISSIPPI BAR

APRIL 2008

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NEW LEGISLATION

The dust is still settling on the 2008 legislative session, but some new laws that will affect real property can already be identified. One bill that passed, S.B. 2382, is the Uniform Environmental Covenants Act. This Act will fill a gap that currently exists between federal and state laws regarding brownfields and risk-based remediation and the common law regarding easements and servitudes. For example, under the common law, questions may arise about whether covenants limiting the use of land are valid if the covenants are in gross rather than appurtenant, and whether such covenants sufficiently "touch and concern" the land so that they run with the land. Similar questions arise if one retains an easement to inspect property to confirm compliance with environmental covenants: is such an easement in gross (arguably a mere license under Mississippi case law) and will it be cut off by a tax sale (the rationale of the *Autumn Woods* case only applies to appurtenant easements)? The UECA answers these questions by confirming the validity of such covenants and easements. The UECA becomes effective July 1, 2008.

It also appears that uniform rules about formatting real estate documents will become law. H.B. 475 imposes formatting requirements on documents filed in the real estate records: for example, documents must be one-sided, have a three-inch margin at the top and three-quarters of an inch on all sides, be printed or typed in font no smaller than eight point, be on white paper, and have all names be typed beneath signatures, and other requirements. Interestingly, it does not require the use of letter-sized paper. These formatting standards will become effective on July 1, 2009. Documents that do not comply with the new formatting requirements can still be filed, but the clerk will charge an extra filing fee of ten dollars. H.B. 475 has been passed by both the House and Senate and sent to the Governor for his signature. Another bill passed by the legislature and signed by the Governor is H.B. 943, which creates a Task Force to Study Uniformity in Real Property Recordings. The Task Force has the duty to study the merits of imposing a statewide uniform system of recording documents relating to real property and the feasibility of electronic recording of documents in the real property records and electronic retrieval of copies of such documents. The task force is scheduled to file a report with the legislature by October 1, 2009 recommending whether or not a uniform system of filing and recording documents relating to real property should be implemented and including a draft of legislation to be introduced in the 2010 legislative session.

Another bill that has become law is S.B. 2075, which amends Section 89-5-33 by adding the following underlined language: “Every surveyor or other person who prepares a legal description of land or who prepares an instrument utilizing an existing description and every person who prepares a deed of trust shall (except as herein provided) include an indexing instruction which shall state the section, township and range and one or more quarter sections....”

One proposal that appears to have died in committee would have required the seller of property to disclose if the property being sold had been used in the production of crystal methamphetamine. Variations of this proposal were proposed in every state this year. The editor is guessing that the realtors supported this proposal. See Miss. Code Ann. § 89-1-527 (broker not liable if broker does not disclose that murder occurred on property or that AIDS victim lived on property or that sex offender lives nearby). Expect to see this proposal adopted in next year’s legislative session.

Efforts to limit certain types of loans and non-judicial foreclosures appear to have failed. S.B. 2825 proposed to limit balloon payments, negative amortization and prepayment penalties in certain loans, and died in committee. S.B. 2436 proposed to require that a lender give the borrower a ninety-day cure period and notice of the right to cure by certified mail before instituting foreclosure. This bill also died in committee.

Several bills were introduced to limit the power of eminent domain. H.B. 591 provided that eminent domain could not be exercised to convert private property to retail, office, commercial, industrial or residential development. S.B. 2822 provided that eminent domain could not be used to take private property for private development, but made an exception for certain economic development projects. Both bills had lots of sponsors and were passed by their respective houses, but died in conference committee. These bills are part of a nationwide reaction to the United States Supreme Court’s decision in *Kelo v. City of New London*. See Steven J. Eagle & Lauren A. Perotti, *Coping with Kelo: A Potpourri of Legislative and Judicial Responses*, 42 Real Prop. Probate & Trust Journal 799 (Winter 2008). We can expect to see similar bills like this being vigorously pushed in the next legislative session. One bill that did pass regarding eminent domain was S.B. 2391. This bill amends the amount must be paid to the landowner when public funds are being used, Miss. Code Ann. § 43-7-3(c), as follows: “The price that shall be paid for real property shall be the lesser of the best negotiated price or the approved appraisal of the fair market value or the price at which the property is offered for sale.” Does this mean that a state agency can’t pay more than the appraised amount just to settle a case? S.B. 2391 also amends sections of the Mississippi Code dealing with subdivision plats and regulation of subdivisions by local governments to provide that the dedication of streets, alleys and other public ways that occurs when a plat showing such streets, alleys and other public ways is the dedication of an easement interest only, and not the fee simple. Consider this amendment in light of *Nettleton Church of Christ v. Conwill*, 707 So. 2d 1075 (Miss. 1997)(discussed in the Spring 1997 edition of the Newsletter). In this case, the Mississippi Supreme Court held that a dedication pursuant to a recorded plat was the dedication of a fee interest. Justice Banks, joined by Justice Prather, dissented in that case on the grounds that under Mississippi law the dedication should be limited to an easement interest. Many real estate lawyers believed that the dissent was the correct reading of the law. It seems to the editor that S.B. 2391, in effect, legislatively overrules *Nettleton Church of Christ v. Conwill*.

**LENDER MUST PROVE THAT BID AT FORECLOSURE WAS
FAIR MARKET VALUE TO COLLECT DEFICIENCY**

Hartman v. McInnis, 2007 WL 4200613 (Miss. Supreme Ct., Nov. 29, 2007). McInnis borrowed money from BancorpSouth to purchase land in Jones County and Forest County, which loan was secured by a first deed of trust on the properties ("McInnis deed of trust"). McInnis sold the properties to Hartman. At closing in November 2003, (a) Hartman paid McInnis part of the purchase price in cash and part in the form of a note from Ronson secured by a deed of trust from Ronson ("Ronson deed of trust"), which note was guaranteed by Hartman; (b) McInnis assigned the Ronson note and Ronson deed of trust to BancorpSouth; and (c) the parties entered into an agreement that Ronson would make his payments on the Ronson note to BancorpSouth, that BancorpSouth would apply Ronson's payments to the McInnis note and pay any excess to McInnis, and that the McInnis deed of trust would be senior in priority to the Ronson deed of trust. Ronson defaulted in payment of his note. McInnis discovered that Ronson was not making payments to BancorpSouth and that BancorpSouth was not taking action to collect from Ronson. McInnis filed suit against Hartman and Ronson alleging breach of contract, and against BancorpSouth for breach of fiduciary duty. McInnis asserted that the agreement for BancorpSouth to collect the payments from Ronson created a fiduciary relationship between McInnis and the BancorpSouth. BancorpSouth filed a cross-claim for judicial foreclosure of the Ronson deed of trust and foreclosed judicially on the properties subject to that deed of trust. BancorpSouth was the sole bidder at the sales, which took place in May 2005, and purchased the properties for \$199,900. BancorpSouth then sought a deficiency from McInnis. The Chancery Court of Forrest County held that BancorpSouth was not entitled to a deficiency because it had not proven the fair market value of the properties upon which it had foreclosed. The Chancery Court held that McInnis, rather than BancorpSouth, was entitled to a deficiency judgment against Ronson and Hartman. On appeal the Mississippi Supreme Court, in an *en banc* decision with a majority opinion by Chief Justice Smith, affirmed in part and reversed in part. The court held that BancorpSouth was not entitled to a deficiency because it had not proven the fair market value of the Ronson properties. In determining its foreclosure bid, officers of BancorpSouth had taken appraisals done in June 2004 (less than an year prior to the foreclosure sales), which showed appraised values of \$297,000, and had discounted the values to \$199,900, based on their inspections of the properties prior to the foreclosure sales. The court concluded that the evidence put on by the bank left the court unable to determine whether the price for which the bank purchased the property at the foreclosure sales was the fair market value. The court also addressed the nature of the assignment of the Ronson note by McInnis to BancorpSouth. Hartman (the guarantor of the Ronson note) argued that since McInnis had assigned the Ronson note to the bank, McInnis did not have standing to bring an action on that note. McInnis therefore asserted that the assignment was a collateral assignment only. While the assignment appeared on its face to be an absolute assignment rather than a collateral assignment, the court determined that the November 2003 agreement showed that the intent of the parties was a collateral assignment. McInnis was entitled to bring an action on the note, but the indebtedness of McInnis to BancorpSouth, which was secured in part by the collateral assignment of the note, had to be satisfied first. Justice Dickinson, joined by Justice Carlson, dissented from the holding that the lender had to prove "fair market value" on the grounds that adopting this higher standard was part of a trend of Mississippi courts increasing the burden on lenders beyond what was required by statutes.

Note 1: The dissent meticulously documents how the courts have gradually increased the lender's burden from proving the absence of fraud to having to prove the fair market value of the property.

Note 2: The majority's opinion puts emphasis on appraisals as establishing fair market value, but there are a number of problems with using appraisals in this context. Appraisals do not take into account the stigma of foreclosure, which affects the value of the property. Because of the involuntary nature of foreclosures, an appraiser often does not have the ability to inspect the inside of a residence. Bitter borrowers who are forced to vacate their homes after foreclosure often trash the property. An article in the March 28, 2008 edition of the *Wall Street Journal* describes this practice, including a surprising use of ferrets.

Note 3: Requiring lenders to bid the fair market value of property being foreclosed upon is a windfall for the borrower because the lender will only be able to apply to the debt the net recovery, if any, after the sale. Suppose that a lender bids in property at its fair market value and then after the foreclosure sale sells the property for that amount. The lender is going to have to pay repairs and maintenance of the property, real estate commissions, closing costs, and probably real estate taxes. So while the defaulting borrower gets credit on his debt for the fair market value, the amount that the lender actually gets to apply to its loan is probably going to be a lesser amount.

Note 4: Three justices joined Chief Judge Smith's majority opinion; Justice Graves concurred in the result only; Justice Carlson joined in Justice Dickinson's dissent on the "fair market value" point; and Justice Easley and Justice Randolph did not participate. Suppose that the next time this issue comes before the court, Justices Easley and Randolph are persuaded by Justice Dickinson's dissent on the fair market value issue, and this time Justice Graves doesn't like the result of applying the fair market value standard. A 5-4 majority then exists for rejecting the fair market value standard.

Note 5: Suppose that the court had found that the bank was owed a deficiency from McInnis. Remember that the foreclosure at issue was of a second deed of trust; the first (McInnis) deed of trust and loan was still out there. What happens to the first deed of trust? The trial court found that BancorpSouth's interests under the first and second deed of trust had merged. The Mississippi Supreme Court sidestepped this issue and stated: "As Mississippi has yet to provide instruction on calculating a deficiency for a wraparound mortgage, and the creation of such guidance is unnecessary for this Court's decision, the Court declines to address that issue here."

GENERAL

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