# Recent Developments in Business, Contract, and Property Law

presented by

*Professor David E. Pierce*

# RECENT DEVELOPMENTS IN KANSAS BUSINESS, CONTRACT, & PROPERTY LAW

by

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***NOTE: This Outline canvasses opinions released by the Kansas Supreme Court and Kansas Court of Appeals as of June 12, 2009.***

## I. BUSINESS LAW

### A. Corporate/Entity Governance Issues

1. **Shareholder failed to carry burden of proof regarding Association president's alleged self-dealing and resulting breach of fiduciary duty to the organization.** ***Becker v. Knoll***, 40 Kan. App.2d 1049, 199 P.3d 786 (2008).

   a. Becker is a shareholder of the Finney County Water Users Association (FCWUA). Becker sued Knoll, the president of the Association, asserting Knoll breached his fiduciary duty owed to the Association by using the services of the Association employee, Morehouse, for Knoll's personal benefit.

   b. FCWUA is a corporation created to maintain and manage 50 miles of irrigation ditches used to divert water from the Arkansas River. Morehouse maintains the ditches for FSWUA. Becker thought Morehouse's time was being improperly diverted by Knoll to work on Knoll's farm.

   c. To prevail the complaining party has the initial obligation to make out a prima facie case of self-dealing. The burden then shifts to the officer to establish their actions were done in good faith.

      (1) Self-dealing is a breach of the duty of loyalty which officers and directors owe to the corporation.

      (2) Must show that the officer's dealings resulted in benefits going to the officer personally that should have gone to the

corporation. In this regard the transaction is "unfair" to the corporation.

d. The evidence merely established that Morehouse did work for Knoll; it did not establish that this created any sort of unfair situation for the corporation, or that any benefits were diverted from the corporation to Knoll.

e. The court holds Knoll rebutted any presumption of unfairness through testimony from Knoll and Morehouse.

2. **By-law can require sale of stock at stated price in the event stockholder becomes involved with a competing business.** ***Kansas Heart Hospital, L.L.C. v. Idbeis***, 286 Kan. 183, 184 P.3d 866 (2008).

a. The controlling interest in Kansas Heart Hospital, L.L.C. (KHH) is held by two corporations, Cardiac Health of Wichita, Inc. (CHW) and Cardiac Associates of Wichita, Inc. (CAW).

b. In 1999 the KHH management committee became concerned that its shareholders (physicians) may be contemplating investment in a competing health care facility. This was perceived to be a conflict of interest for any CHW shareholder that may invest in a competing facility.

c. In response to this concern, in 2000 the bylaws of CHW were amended to provide:

> "No shareholder of the corporation shall be permitted to own either directly or indirectly through any means of ownership, all or any portion of a ***competing health care facility located within one hundred (100) miles of the city limits of Wichita, Kansas***. A 'competing health care facility' is defined as any medical hospital or facility specializing in cardiac, cardiothoracic, or vascular care. . . . ***In the event a shareholder violates the terms of this restriction, the corporation may compel redemption of the shareholder's stock*** pursuant to Section 1.5(b) of these bylaws, however, the maximum redemption price shall not exceed Five Hundred Twenty-Five Dollars ($525.00) per share, increased or decreased by any percentage change in the Consumer Price Index. The intent is to prohibit ownership of a competing health care facility, not a limitation of anyone's group practice or facilities integrated within the practice. The Board of Directors shall issue such interpretations as are necessary to carry out

the intent of this restriction."

d. In 2004 several doctors, who were CHW shareholders, invested in Kansas Medical Center (KMC) which was determined to be "a competing health care facility" with KHH within 100 miles of Wichita.

e. In January 2005 the CHW Board redeemed the doctor's shares relying on its bylaw redemption authority.

f. In February 2005 the CAW Board redeemed the doctor's shares in CAW because a CAW bylaw requires ownership of CHW stock in order to own CAW stock.

g. The stock redemptions do not affect the doctor's staff privileges at KHH; they need not own an interest in KHH to practice at KHH.

h. Issue: Can a restriction on stock ownership, that provides for redemption by the company, be imposed through a bylaw instead of an amendment to the articles of incorporation?

(1) The court distinguishes between restrictions on a "class" of stock and restrictions targeted at the "holder" of the stock on an individual, as opposed to class, basis.

(2) K.S.A. §§ 17-6002(a)(4), 17-6401(a), and 17-6602 all contemplate that restrictions on a class of stock must be addressed in the articles of incorporation.

(3) K.S.A. § 17-6426(b) allows for "ownership restrictions" to be "imposed either by the articles of incorporation or by the byaws or by an agreement among any number of security holders or among such holders and the corporation."

(a) This section also states: "No restriction so imposed shall be binding with respect to securities issued prior to the adoption of the restriction unless the holders of the securities are parties to an agreement or voted in favor of the restriction."

(b) All of the affected individuals in this case not only voted in favor of the bylaw amendment, but also further expressed their approval on a "Voting Form."

(4) The court concludes:

"[T]he challenged provision operated only against certain stockholders (in the event of a stockholder investing in a competing health care facility), not against an entire class of stock. Because of this, the district court correctly classified the provision as a restriction on the amount of stock that could be owned. In other words, under the express language of the bylaw provision, certain persons were not permitted to own shares of CHW stock; their ownership was restricted. Thus, the provision fell within K.S.A. 17-6426(b) as a restriction "on the amount of the corporation's securities that may be owned by any securities holder."

(5) Therefore, the restriction could be imposed using the bylaw instead of an amendment to the articles of incorporation.

(6) The context of the transaction, and viewing the situation as would be "understood by a hypothetical reasonable third party" the word "redeem" in CHW's bylaws means "purchase" the holder's interest as would be the case in a buy-sell agreement.

(a) It is not the sort of statutory redemption that must be authorized by the articles of incorporation.

(b) "The reasons that would trigger the reacquisition of the stock are not within the control of the board of directors and would not be targeted at a class of stock. Rather, it would be targeted at the holder of the stock who no longer meets eligibility requirements as defined in the contract among the shareholders."

(7) "We conclude the use of the word 'redemption' in CHW's bylaw section 1.5(e) is susceptible to more than one meaning and, when considered in the context of the bylaw and Kansas' statutes, would be understood by a reasonably prudent person to mean CHW had the power to purchase the stock at the predetermined price. Therefore, section 1.5, as a restriction on transfer and ownership and allowing for CHW to reacquire the stock, was valid and enforceable and did not violate K.S.A. 17-6401(b) or K.S.A. 17-6410."

i. Issue: In determining whether the bylaw applied to the doctors' investment in KMC (was KMC a "competing health care facility" before it was contructed?), will the actions of the board of directors for CHW be evaluated applying the ***business judgment rule***?

(1) The business judgment rule is:

> "The presumption that in making business decisions not involving direct self-interest or self-dealing, corporate directors act on an informed basis, in good faith, and in the honest belief that their actions are in the corporation's best interest. The rule shields directors and officers from liability for unprofitable or harmful corporate transactions if the transactions were made in good faith, with due care, and within the directors' or officers' authority."

(2) First issue: is this even a "business judgment" issue? The court notes the bylaw trigger was tied to the board's decision whether to redeem the CHW shares of stock. If there had been a violation of the bylaw, then the board had to determine how to respond.

(3) Court relies upon a 2001 Court of Appeals decision, *Gray v. Manhattan Medical Center, Inc.*, for the propositions:

(a) "The business judgment rule gives a corporation's directors the authority to interpret and apply the bylaws and the lease in the corporation's best interest."

(b) "[T]here was a dispute regarding the interpretation of the lease and bylaws. . . . The fact that [the directors] chose a course of action Gray disagrees with does not affect the applicability or reduce the protection of the business judgment rule."

(4) Interestingly, the bylaw itself states: "The Board of Directors shall issue such interpretations as are necessary to carry out the intent of this restriction."

(5) The court concludes: "The decision made by CHW's board of directors was a business judgment decision."

j. Accepting that the business judgment rule applies, was the board's action made by disinterested directors, acting on an informed basis, in good faith believing the decision was in the best interest of the corporation?

(1) Disinterested Directors. The fact they may benefit proportionally with all remaining shareholders by the repurchase of the doctors' shares does not make them "interested" or subject to any sort of conflict.

"A director is interested 'where the director has a financial or pecuniary interest in a transaction *other than that which devolves to the corporation or to all of the shareholders generally.*'"

(2) Informed Directors (duty of due care). The facts indicate the directors were provided the necessary information to properly evaluate the issues prior to making their decision.

(3) Good Faith Actions. Issue is not one of "fair value," as in a cash-out merger, but rather good faith application of the contractual provisions of the bylaws. There was a good faith belief that KMC was a competitor and that the bylaw provisions were triggered.

## B. Banking Law

1. **Lender waived right to exercise rights under acceleration clause immediately following a period of accommodating borrower's late payments.** ***Foundation Property Investments, LLC v. CTP***, 286 Kan. 597, 186 P.3d 766 (2008).

a. CTP borrowed $96,000 from Foundation to purchase a truck stop. The promissory note provided for payments of $673.54 each month from 2004 to 2009, at which time the balance would be paid in full. However, the note provided that if the monthly payments were not paid on the date due "the whole amount shall become immediately due and payable at the option of the holder without notice."

b. The first four payments were made in a timely manner followed by nine late payments.

(1) Following the ninth late payment Foundation informed CTP

that it was exercising its option under the acceleration clause to require payment of the balance due on the note.

(2) CTP argued Foundation had waived its right to insist on timely payment by accepting the nine late payments without objection.

(3) Foundation argued it had waived nothing because each month it had the "option" to determine whether it would trigger the acceleration clause and failing to exercise its option during the nine-month period was not a waiver.

c. The Court notes the difference between an "acceleration clause" and an "anti-waiver clause."

(1) Rejecting Foundation's argument that its "optional" acceleration clause avoided the need for an anti-waiver clause, the Court provides the following drafting advice:

"[W]e strongly encourage the use in Kansas of clearly stated anti-waiver provisions . . . ."

(2) Dissenting Justice Beier believed the optional acceleration clause avoided the waiver issue and therefore additional language, in the form of an "anti-waiver clause," is not necessary.

d. After determining the optional acceleration clause was not an anti-waiver clause, the Court concludes: "Nine straight months of Foundation's accepting late payments, without objection, is a waiver of the right to accelerate."

e. The next question is whether the waiver is a total surrender of the right to accelerate, or only a temporary limitation on the right. To resolve this issue the Court accepts CTP's concession that "'Foundation can "revive" its right to accelerate the Note if it notifies CTP that future payments will no longer be accepted after the due date.'"

f. **COMMENT:** It appears a "good faith" analysis could harmonize the positions of the Court and dissenting Justice Beier.

(1) Although Foundation had the right – the option – to decide

whether to accelerate, by its actions it may have led CTP to reasonably believe timely payment was not required.

(2) If this was the case, Foundation then became obligated to give CTP adequate notice that it may, in the future, elect to trigger its acceleration rights if a future payment is not timely.

(3) This would seem to be the proper role for the obligation of good faith which applies to the performance *and enforcement* of the contract.

(a) The surrounding facts and circumstances, including the express language of the contract, will be used to determine whether CTP reasonably believed timely payment was not required.

(b) The existence of such a good faith belief would limit Foundation's ability to freely exercise its acceleration rights because of a late payment.

(c) However, if the express contract language indicated Foundation, after an extended period of accepting late payment, could nevertheless exercise its acceleration rights without advance notice, it will make it difficult for CTP to establish any sort of "reasonable belief" on the issue. This is consistent with a proper good faith analysis because the parties can always limit the need for a good faith filler by expressly addressing the matter in the contract.

2. **Purchase money mortgage holder not affected by tax lien held by the State of Kansas against buyer/mortgagor of property.** ***American General Financial Services, Inc. v. Carter***, 39 Kan. App.2d 683, 184 P.3d 273 (2008).

a. 2001: Jeff apparently failed to pay his sales taxes, resulting in the Kansas Department of Revenue (KDR) filing a tax warrant against Jeff in the amount of $266,550.23.

b. 2004: Jeff and his wife purchased a home which they financed with a purchase money mortgage through American General Financial Services, Inc.

c. 2005: the KDR filed two additional tax liens against Jeff.

d. 2006: Jeff and his wife defaulted on their home mortgage obligations, causing American to foreclose on its mortgage.

e. The property was sold at a foreclosure sale and American and KDR are competing for the proceeds of sale.

f. The district court awarded KDR priority for its 2001 tax warrant, then American's first and second mortgages obtained in 2004, then KDR for its 2005 liens.

g. The Court of Appeals reverses the trial court and holds American's purchase money mortgage has priority over KDR's tax warrant and lien.

(1) Characterizing the issue as one of "first impression in Kansas," the court first looks for guidance from K.S.A. § 58-2305 which states: "A mortgage given by a purchaser to secure the payment of purchase money shall have preference over a prior judgment against such purchaser."

(2) K.S.A. § 79-3617 treats an unsatisfied tax warrant as the equivalent of a "judgment."

(3) The court is careful to point out what this case is not about: we are not dealing with a lien on property being *sold by a seller*. Instead, we are dealing with a lien against a *buyer* of property who has no interest in the property until it is acquired using the mortgagee's money.

h. Judge McAnany, writing for the panel, does an excellent job of analyzing the nature of the purchase money mortgage and the priority it has been given by courts when others seek to gain priority in the very property the mortgagee has caused to be brought into the debtor's pool of assets. As the court explains:

"[A]t the time of closing the buyer does not acquire title to the property and *then* the purchase money mortgage attaches to and becomes a lien on the property. To the contrary, at closing the buyer acquires title to the property *already encumbered* by the purchase money mortgage. Until the Carters bought their home, there was no real property to which KDR's tax lien could attach. At the moment

the Carters acquired title to their home, it was already encumbered by American's purchase money mortgage. At that point, KDR's tax lien attached to the property, but this occurred *after* the creation of American's purchase money mortgage encumbrance. Thus, American's first mortgage has priority over the Carter's other liens." (Emphasis by the court).

3. **Assignee of loan that is not a qualified "supervised lender" is prohibited from collecting on a UCCC "supervised loan."** ***Independent Financial, Inc. v. Wanna***, 39 Kan. App.2d 733, 186 P.3d 196 (2008).

   a. Ron and Susan took out a first mortgage to purchase their home which was held by Countrywide Mortgage. Subsequently they took out a second mortgage with Ditech Funding Corporation, for $85,000, with an interest rate of 13.75%.

      (1) This second mortgage was subject to the Kansas Uniform Consumer Credit Code (KCCC) as a "supervised loan" because it was a consumer loan with an annual percentage rate exceeding 12%.

      (2) Although Ditech was a qualified "supervised lender" under the KCCC, Ditech assigned the note and mortgage to Independent Financial, Inc. (IFI), which is not a "supervised lender."

   b. At the foreclosure proceeding, IFI asserted rights under a workout agreement it entered into with Ron, Susan, and their other creditors. Another creditor sought dismissal of IFI's claim in the foreclosure proceeding because it was not a licensed supervised financial organization.

      (1) The district court agreed and held IFI was prohibited from collecting on the loan and foreclosing on the mortgage because it was not properly licensed to ensure its collection procedures are within regulatory limits.

      (2) Affirming the district court, the Court of Appeals concludes that K.S.A. § 16a-2-301(2) prohibits IFI from collecting on, or enforcing, the loan so long as IFI is not a licensed supervised lender.

4. **Judgment liens can not attach to homestead or impair priority of purchase money mortgage.** ***Deutsche Bank National Trust Company v. Rooney***, 186 P.3d 820, 39 Kan. App.2d 913 (2008), *review denied* (Nov. 4, 2008).

   a. 2004: Thomas entered into a mortgage on his residence in December; earlier in May 2004 Thomas ceased making court-ordered support payments to Kathleen. Nu-Dell obtained a judgment against Thomas in 2004 prior to the December 2004 mortgage.

   b. 2005: The mortgagee, Deutsche Bank, sought to foreclose against Thomas' residence because Thomas failed to make the payments required under his note and mortgage.

      (1) The Bank's mortgage was consensual and an express exception to the homestead exemption; therefore the Bank's lien attached to the homestead property and the Bank could force a sale of the homestead property to pay its debt.

      (2) The liens of Kathleen and Nu-Dell, however, were non-consensual judgment liens encompassed by the protection provided Thomas under the homestead exemption. Their liens would not attach to the property, nor could they force a sale of the property to pay their liens.

   c. Kathleen and Nu-Dell, the judgment creditors, assert their liens could attach to Thomas' homestead once *the Bank* commenced foreclosure proceedings.

      (1) They further argue that because their liens pre-date the Bank's mortgage, they have priority to any proceeds from the foreclosure.

      (2) Kathleen and Nu-Dell assert changes to the Kansas homestead statutes give them the ability to acquire liens against the homestead which, although as judgment creditors *they* cannot force a sale of the homestead, once another party, such as the Bank forces a sale, then their previously non-attaching liens attach and date back to the date the lien accrued.

   d. The court, relying upon *Morris v. Ward*, 5 Kan. 239 (1869), rejects the judgment creditors' theory and holds that only those liens specifically excepted from the homestead exemption can attach to

homestead property.

(1) The liens encompassed by the exception are those that are: consensual, for taxes, for purchase money to acquire the homestead, and for improvements to the homestead.

(2) The court reaffirms the protective focus of the *Morris* opinion, noting that allowing a lien to attach at some future date "would prevent families from changing homesteads and perhaps prohibit them form acquiring new homesteads – an outcome contrary to the policy behind the homestead protection, which was to protect families from destitution."

(3) Therefore, the liens held by Kathleen and Nu-Dell, as judgment creditors of Thomas, cannot be satisfied out of funds generated by a foreclosure sale of Thomas' homestead property.

e. **COMMENT:** Although not the focus of this opinion, it would appear if there are any excess funds remaining after payment of the Bank, Thomas could protect them from levy by Kathleen and Nu-Dell by using the money to acquire a new homestead. See *Mitchell v. Milhoan*, 11 Kan. 617 (1873) (proceeds from sheriff's sale); *In re Daniels*, 65 B.R. 703 (1986) (proceeds from involuntary transfer in divorce proceeding). *See generally*, Roger L. Theis & Karl R. Swartz, *Kansas Homestead Law*, 65 JOURNAL OF THE KANSAS BAR ASSOCIATION 20 (April, 1996).

## C. Commercial Law

### 1. Implied warranty of merchantability applies to air conditioner on 10-year-old used car. ***Hodges v. Johnson***, 288 Kan. 56, 199 P.3d 1251 (Kan. 2009).

a. Johnson is a used car dealer. Johnson sold Hodges a ten-year-old Mercedes S320 automobile with 135,945 miles on it, which, according to Hodges, Johnson represented to be "just pretty much a perfect car." When Hodges discovered the air conditioner was not working properly he demanded that Johnson fix it. Johnson refused and Hodges sued in small claims court for $3,474, the estimated cost of repair. The vehicle purchase price was $15,900.

(1) Hodges prevailed in small claims court and Johnson appealed

to district court.

(2) The district court also held for Hodges but refused to award attorney fees under K.S.A. § 61-2709(a) as a prevailing appellee from a small claims court award.

(3) The Court of Appeals, in a 2/1 decision, reversed the trial court, holding the implied warranty of merchantability on a used vehicle extends only to major components that are necessary for use of the vehicle to provide transportation.

(4) The Supreme Court reverses the Court of Appeals and holds the trial court properly determined, as a matter of fact, that the air conditioning system of the vehicle was properly encompassed by the implied warranty of merchantability.

(a) The Court, however, reverses the trial court's refusal to award attorney fees to Hodges, noting K.S.A. § 61-2709 imposes a mandatory duty to award attorney fees when the appellee is successful on appeal.

(b) Although the Court remands the case to the trial court to determine the award of attorney fees incurred at trial, the Court, under Supreme Court Rule 7.07(b), awards attorney fees and expenses of $4,106.50 for the cost of the appeal to the Supreme Court.

b. This case will be of interest to commercial lawyers because of Justice Davis' discussion of the implied warranty of merchantability as applied to used goods.

(1) To determine whether the implied warranty has been breached, the initial task is to determine whether, under the facts and circumstances of the transaction, the failure of the air conditioner to work is a matter encompassed by the seller's warranty obligation.

(2) After hearing all the facts, the trial court concluded the air conditioner was covered by the seller's implied warranty.

(3) To establish a breach of the implied warranty, Hodges must show "that the purchased goods were defective, that the defect was present when the goods left the seller's control, and that

the defect caused the injury . . . ."

(4) The Court holds there was substantial competent evidence presented to the trial court to support its conclusion that the car was defective because it had a bad air conditioner, the air conditioner did not work properly at the time the car was sold to Hodges, and Hodges was injured by the amount it would take to fix the air conditioner.

c. **COMMENT:** Although it is arguable whether the "just pretty much a perfect car" statement attributed to Johnson gave rise to an express warranty, the trial court and Supreme Court were able to use the statement to address the factual issue regarding the scope of the implied warranty of merchantability.

(1) For example, with a used car that has an air conditioner, and which the seller indicates is "just pretty much a perfect car," it is reasonable to conclude the implied warranty for this used car would encompass the air conditioner.

(2) This statement took on even greater significance when Johnson indicated he had been driving the car as his personal vehicle for almost two years.

d. **COMMENT:** This case is also important because of the efficacy it gives to a favorable ruling in small claims court.

(1) Anecdotally it would appear that the "little guy" or "consumer" will often prevail against the "big guy" in small claims court as judges seek an appropriate resolution of claims made against a supplier or dealer.

(2) If the "little guy" loses in small claims court, they will most likely let it end at that point, because the amount of their claim is still "small" and if they want to appeal to district court they will most likely need to invest substantial sums in attorney fees.

(3) When the "big guy" is the appellant, they can more readily invest in attorney fees to take the battle to the district court. This is where the mandatory attorney fees statute will have the most effect as a deterrent to those who could otherwise afford to prosecute an appeal of an adverse ruling.

(4) Because a small claims judgment will have little or no practical precedential impact on the "big guy," they may be willing to forego appeals of adverse rulings.

(a) This provides a workable mechanism to compensate individuals who have claims at or below the $4,000 small claims jurisdictional threshold.

(b) The mandatory attorney fees against an unsuccessful small claims appellant forces the party to carefully evaluate whether they should just accept the judge's ruling and move on.

(c) The Court holds there is a rational basis for imposing the risk of attorney fees on the appellant, and not the appellee, in order to "keep expenses low and allow for expedited resolutions of small claims . . . ."

2. **Holder in due course that had fully performed by paying value on check is not subject to UCC 3-302(d) set-off.** ***Hurst Enterprises, LLC v. Crawford***, 40 Kan. App.2d 1018, 197 P.3d 882 (2008).

a. Cactus Roofing, LLC issued a $4,768.47 check to Tomas Hernandez for roofing work.

(1) Hernandez took the check to Hurst Enterprises, LLC, d/b/a Mr. Payroll Check Cashing, and cashed the check less a 1% check cashing fee of $47.68.

(2) Three days after the check had been paid by Hurst, Cactus placed a stop payment on the check because Hernandez had not completed the roofing job properly.

(3) Hurst was not paid on the check and brought suit to recover the amount due.

b. At trial, the court determined Hurst was a holder in due course under K.S.A. §84-3-302, but was subject to a subsection (d) set-off because Hernandez had only partially performed the roofing work, resulting in Cactus having to spend $4,500 to complete the contracted work. Therefore, the trial court awarded Hust $268.47 ($4,768.47 - $4,500).

c. The Court of Appeals reverses holding the subsection (d) portion of

UCC § 3-302 focuses on the partial performance of the holder in due course, not the payee who presented the check for payment.

(a) In this case Hurst had fully performed by paying the full sum of the check, less a check-cashing fee.

(b) There was no partial performance on the part of the holder in due course, so subsection (d) was never triggered.

(c) As a holder in due course, Hurst is entitled to recover the full amount of the check, $4,768.47, from Cactus.

## II. CONTRACT LAW

### A. Formation and Enforceability

1. **Supreme Court makes clear that validity of liquidated damages clauses governed by Kansas law will be evaluated based upon anticipated damages at the time contract entered into without regard to how the agreed liquidated damages may ultimately compare to the actual damages.** ***Carrothers Construction Company, L.L.C. v. City of South Hutchinson***, ____ Kan. ____, 207 P.3d 231 (May 22, 2009).

a. During last year's Recent Developments program we discussed this case and noted the Court of Appeals had taken a two step analysis which evaluates the liquidated damage figure by first applying a prospective analysis to determine if it is a reasonable prediction of damages (Step #1). This is then followed by Step #2 where a retrospective analysis is applied to see how the liquidated damage figure compares to the actual, known damages the party suffers.

(1) This means that a reasonable prediction of damages made at the time of contracting could be overturned if it did not, in fact, compare reasonably to what are subsequently determined to be the actual damages.

(2) Such an approach defeats the underlying purpose and benefits of a liquidated damages clause by prompting litigation of damages in every case where it can be argued the parties' reasonable prediction does not reflect what all agreed at the time could not be predicted with accuracy.

b. Discussing the *Kansas Heart Hospital* case last year, I observed:

"The court's adoption of the additional "retrospective" inquiry may not be consistent with the route the Kansas Supreme Court may ultimately follow."

(1) "For example, on May 16, 2008 the Kansas Supreme Court issued its opinion in ***Kansas Heart Hospital, L.L.C. v. Idbeis***, Case No. 97,131, 2008 WL 2065843 (Kan., May 16, 2008), where the court considered whether a bylaw requiring a stockholder to sell its stock back to the company at a pre-determined price was an illegal penalty.

(2) The court, without discussion, rejects a retrospective analysis stating: "The determination of whether there is a penalty does not depend on speculating on the performance of investments." To support this proposition it cites the *TMG Life* case, a 1995 Court of Appeals case, and quotes the following passage from *TMG Life*: "The reasonableness of a liquidated damages clause should be determined as of the time the contract was executed, not with the benefit of hindsight."

(3) Because the court does not address the precise issue of a prospective and retrospective inquiry, the context of its statement in *Kansas Heart Hospital* may be to merely highlight that there is a prospective analysis – not that a court would never evaluate the situation using a retrospective analysis. **This issue apparently remains open for the Kansas Supreme Court – although the Kansas Court of Appeals has clearly adopted a prospective and retrospective analysis in the *Carrothers* case."**

c. By accepting review of the *Carrothers* case, the Court, although affirming the Court of Appeals' decision, uses the opportunity to overrule prior Court of Appeals use of a two-step prospective and retrospective analysis of liquidated damages clauses.

d. The City contracted with Carrothers to build a new sewage treatment plant for $5,618,000. Included in the contract was a liquidated damages clause which provided for payment of $850/day for each day the project ran past the defined "substantial completion" and "final completion" dates.

(1) The City's engineering firm, MKEC Engineering Consultants,

Inc. (MKEC), conducted an analysis of how a delay could impact the City and used this analysis to recommend the $850/day figure.

(2) The City withheld $145,350 from its final payment to Carrothers as liquidated damages for 170 days of delay before "substantial completion" and 1 day of delay before "final completion."

e. Was the "substantial completion" date properly determined?

(1) Although the City occupied and began operating the new facility in November, it was not declared substantially complete until January of the following year. Carrothers argues it was substantially complete when the City occupied and commenced operating the facility in November.

(2) The Court finds there were a number of significant items that needed to be completed, including completion of the computerized operating system. The City was operating it manually from November to January; a major part of the project was to have it be computer-operated.

(3) Also, Carrothers fails to address the express clause in the contract which delegates to the project engineer the authority to determine when the work would be deemed "sufficiently complete in accordance with the Contract Documents."

(a) The project engineer did not do this until January.

(b) There is no assertion the project engineer acted in bad faith in not certifying completion in November.

f. Was the liquidated damages clause enforceable, or was it an unenforceable penalty?

(1) "The distinction between a contractual penalty and a provision for liquidated damages is that a penalty, in effect, is a security for performance, while a provision for liquidated damages requires a sum certain to be paid in lieu of performance."

(2) The burden of proof is on the party challenging a liquidated

damages clause.

(3) "[W]e [the Court] promote a public policy favoring settlement and avoidance of litigation, and allowing parties to make, and live by, their own contracts."

(4) The Court quotes from *Erickson v. O'Leary*, 127 Kan. 12, 273 P. 414 (1929), the basic analysis to be followed:

"The instrument must be considered as a whole, and the situation of the parties, the nature of the subject matter and the circumstances surrounding its execution taken into account. There are two considerations which are given special weight in support of a holding that a contractual provision is for liquidated damages rather than a penalty – the first is that the amount stipulated is conscionable, that it is reasonable in view of the value of the subject matter of the contract and of the probable or presumptive loss in case of breach; and the second is that the nature of the transaction is such that the amount of actual damages resulting from default would not be easily and readily determinable."

(5) The Court makes it clear that any sort of retrospective analysis is improper.

(a) "We disagree and hold the retrospective analysis is unnecessary in determining whether a liquidated damages clause is a penalty."

(b) "The better test, we believe, is to determine the reasonableness of a liquidated damages clause as of the time the contract was executed, not with the benefit of hindsight."

(c) "As noted previously by this court, a liquidated damages clause in a contract is an advance settlement of the anticipated actual damages arising from a future breach."

(d) "Such provisions allow contracting parties to protect themselves against the difficulty, uncertainty, and expenses that necessarily follow judicial proceedings when trying to ascertain actual damages."

(e) "[O]ur decision in this case is intended to lay aside any further doubt and embrace a prospective analysis as the sole basis for evaluating a liquidated damages provision in a contract. To the extent any prior decisions of the Court of Appeals have contributed to that doubt by adding a retrospective test in their determination of this issue, they are overruled as to this limited point."

(6) Applying the Court's analysis to the facts, it concludes that at the time the contract was entered into damages were not readily calculable and the $850/day was a reasonable estimate of damage to the City in the event of a delay.

(7) Another consideration the Court injects: "[W]e are dealing here with a contract for the construction of public utility service facilities. It is uniquely difficult to calculate damages to the general public interest caused by a contractor's breach of its agreement to provide public improvements. This should be an important consideration in such cases and weigh favorably in finding a liquidated damages provision to be reasonable. Kansas has long recognized the protection of the public interest is a proper consideration in determining validity of a liquidated damages provision."

g. To illustrate the Court's pure prospective analysis, Carrothers argued that the $850 for the one day delay between "substantial" and "final" completion was clearly a penalty because the City suffered no actual damages.

(1) The event that was required to move from substantial completion to final completion was delivery of some operating manuals. Carrothers argued the City was not damaged in any way by Carrothers failing to deliver the operating manuals for a day.

(2) This is where the prospective vs. retrospective analysis is vividly illustrated.

(3) It does not matter that there were, in fact, no actual damages.

(4) "The test for this contractual provision's reasonableness is whether (1) ***at the time of contracting*** it would appear

conscionable to assess $850 per day in liquidated damages for the period of time between substantial and final completion in view of the value of the contract and the probable or presumptive loss in case of a breach; and (2) actual damages for that time period would be difficult to calculate." (Emphasis added).

2. **Prepayment provision in commercial loan agreement was enforceable by lender and lender was entitled to contractual attorney fees associated with defending validity of prepayment provision.** ***Santa Rosa KM Associates, LTD., P.C. v. Principal Life Insurance Company***, ____ Kan. App.2d ____, 206 P.3d 40 (April 24, 2009).

a. 1991 Dennis Eskie, owner of the Santa Rosa Shopping Center, borrowed $6,375,000 from Principal, giving Principal a promissory note and mortgage. The note contained a "make whole premium" provision which required Eskie to compensate Principal for future lost interest revenue in the event Eskie elected to prepay the loan. The note contained a "greater of" formula for calculating the prepayment fee.

b. 1998 Santa Rosa KM Associated, LT, P.C. purchased the shopping center from Eskie and assumed the note and mortgage. Principal agreed to accept Santa Rosa on the note and mortgage; the prepayment provisions were not modified, nor were they the object of negotiations.

c. 2005 Santa Rosa considered prepayment of the $4,865,142.24 balance due on the note. Under the prepayment fee formula the "make whole premium" due Principal would be $1,636,268.96. This prompted Santa Rosa to commence a declaratory judgment action contending the prepayment fee was unenforceable.

d. The trial court held for Principal but refused to enforce the contractual attorney fees provisions in the note and the mortgage. Santa Rosa appealed enforcement of the prepayment fee and Principal cross-appealed the denial of attorney fees. The Court of Appeals holds the prepayment fee and attorney fees provisions of the loan agreement are both enforceable.

e. The prepayment fee does not violate public policy.

(1) All the debtors were sophisticated business people.

(2) The court comments on the purpose of the clause as follows:

"The 'make whole premium' was designed to avoid a 'heads I win, tails you lose' outcome when the election to prepay the loan is entirely in the borrower's hands. In a period of rising interest rates, it is in Santa Rosa's interest (and to Principal's disadvantage) to continue making payments at the favorable interest rate on the existing loan. ('Heads I win.') In a period of falling rates, it is in Santa Rosa's interest (and to Principal's disadvantage) to refinance the debt at a lower interest rate, thus forcing Principal to invest the proceeds at a lower rate of interest. ('Tails you lose.'). The 'make whole premium' provision has the effect of offsetting the downside risk when the borrower, after enjoying a favorable interest rate on the loan during periods of rising interest rates, unilaterally elects to prepay the loan when interest rates fall."

(3) "Rather than offending our public policy, such a provision would seem to lend stability and predictability to loan transactions, particularly in commercial loans involving a sophisticated and experienced borrower, such as here. It preserves the benefit to the lender of the bargain made at the time of the loan. It commits the borrower to that same bargain independent of fortuitous fluctuations in interest rates."

(4) The Court indicates that the reasonableness of the prepayment fee should be evaluated at the time the parties entered into the contract, not the time when it is triggered. Borrowing from the Court's analysis in the *TMG* case on liquidated damages, the Court states: "'the reasonableness of a liquidated damages clause should be determined as of the time the contract was executed, not with the benefit of hindsight."

(5) Although Santa Rosa is able to demonstrate that the prepayment formula was not the best estimate of Principal's actual loss:

"[I]t was not considered so onerous in 1998 as to cause Santa Rosa not to ratify it. Viewing the transaction prospectively from 1998 [when the loan agreements were amended to add Santa Rosa for Eskie] and without the benefit of hindsight from 2005 and considering the court's admonition in *TMG*,

Santa Rosa fails to show that the formula is so unreasonable as to render it unenforceable."

(6) **COMMENT:** Freedom of contract includes the right to make what may turn out to be a very "bad" deal or a very "good" deal.

f. The prepayment fee is not unconscionable.

(1) The same sort of equities are considered regarding Santa Rosa's argument the prepayment fee provision is unconscionable.

(2) Court relies upon *Wille v. Southwestern Bell Telephone Co.* where unconscionability is defined in a manner which tends to limit it to the most abusive of consumer sales practices: fine print boilerplate, unsophisticated consumer, gross cost-price disparity, denial of basic rights and remedies to the buyer, incomprehensible phrasing, and a clear overreaching by the seller of the underprivileged, uneducated, and often illiterate buyer.

(3) Rarely will parties to a commercial transaction fit the sort of consumer-oriented unconscionability elements of *Wille*.

(4) The Court notes:

"We have no doubt that it is possible that the amount of a 'make whole premium' when coupled with evidence that the lender unfairly exploited an unsophisticated borrower could lead to a finding of unconscionability. However, those are not the circumstances here. Under the uncontroverted facts before us, the amount of the 'make whole premium' does not in itself render this provision unconscionable."

(5) **COMMENT:** If the Court applied the Kansas Supreme Court's teachings in a more recent unconscionability case, *Kansas Baptist Convention v. Mesa Operating Ltd*, 864 P.2d 204 (Kan. 1993), it could have easily held the clause was unconscionable. The Court of Appeals, however, wisely avoided the *Kansas Baptist* analysis which fails to evaluate the contact terms as of the date they were entered into – as opposed to the situation decades later when suit was filed.

The parties in *Kansas Baptist Convention* were sophisticated, represented by sophisticated legal counsel, and the perceived "weaker" party actually set the structure of the deal due to special limitations it had to address in other testamentary documents. For a critique of the *Kansas Baptist Convention* case see: David E. Pierce, *The Renaissance of* Law *in the* Law of *Oil and Gas: The Contract Dimension*, 42 WASHBURN L. J. 909, 917-23 (2004).

g. The attorney fees clauses in the note and mortgage are enforceable because the 1994 amendment to K.S.A. § 58-2312 applies to this transaction and should not be limited to what are strictly viewed as costs associated with a "collection" action.

(1) Prior to the 1994 amendment to K.S.A. § 58-2312, no debt instrument could provide for the payment of attorney fees.

(2) K.S.A. § 58-2312, after the 1994 amendment, and in its current form, provides:

"Except as otherwise provided by law, any note, mortgage or other credit agreement may provide for the payment of reasonable costs of collection, including, but not limited to, court costs, attorney fees and collection agency fees, except that such costs of collection: (1) May not include costs that were incurred by a salaried employee of the creditor or its assignee; and (2) may not include the recovery of both attorney fees and collection agency fees."

(3) Does the statute apply to this note and mortgage? Although the original note and mortgage were entered into in 1991 before the amendment, they were amended in 1998 when Santa Rosa agreed to be bound by their provisions.

"Accordingly, the current form of K.S.A. 58-2312 applies to this transaction, and the total ban of attorney fees in the earlier version of K.S.A. 58-2312 does not apply."

(4) Is a declaratory judgment action, pursued where there has been no default, covered by the attorney fees statute? Yes. The Court reasons as follows:

"While the statute refers to attorney fees in collection actions, the legislative history is devoid of any suggestion that

attorney fees in promissory notes should be limited to collection action to the exclusion of declaratory judgment actions such as the one now before us. . . . The legislature was lifting the blanket prohibition and restoring freedom of contract to parties to negotiate on the issue of attorney fees, particularly in a commercial context such as we find here."

(5) **COMMENT:** Another way to view the statute is that the goal was to return Kansas to the American Rule "except as otherwise provided by law" – such as limitations in the UCCC, the Residential Landlord Tenant Act, the Consumer Protection Act, etc. It would also include the special limitations noted in items (1) and (2) of 58-2312 regarding particular fee items.

h. Were the attorney fees clauses broad enough to encompass the declaratory judgment action? Yes. The action fell within the scope of the "in any way affecting or pertaining to this mortgage, the Note or the premises."

3. **Statutory "One Call" duties cannot be avoided by contract.** ***Double M Construction, Inc. v. State Corporation Commission***, 288 Kan. 268, 202 P.3d 7 (2009).

a. Double M Construction, Inc. was the excavation subcontractor for Double J Pipeline, LLC.

(1) Pursuant to their contract, Pipeline, the prime contractor, agreed to identify existing pipelines in the area so they could be safely crossed when Double M excavated.

(2) Pipeline contacted Kansas One Call to coordinate the spotting of existing utilities in the excavation path. Apparently Pipeline failed to communicate with Double M, which resulted in Double M excavating the area before it had been marked through the Kansas One Call system.

b. Double M struck a high-pressure natural gas transmission line resulting in the death of a Double M employee and property damage.

(1) The Kansas Corporation Commission assessed a $25,000 penalty against Double M for failing to comply with the Kansas One Call statutes.

(2) Double M's defense was that it had a contract with Pipeline which required Pipeline to locate utilities before Double M's excavation.

c. The Court rejects Double M's contract defense stating: "Unless a statute expressly or implicitly allows for delegation, statutory duties imposed on one party generally may not be delegated by contract to another party."

(1) Double M was the "excavator" required to comply with the Kansas Underground Utility Damage Prevention Act by following the Kansas One Call procedures.

(2) Double M's delegation of this responsibility through its contract with the prime contractor does not relieve Double M from its statutory duties.

(3) Although Double M may have tort or contract claims against the prime contractor for its failure to communicate the utility marking status to Double M, that will not affect Double M's liability for its failure to comply with the statute.

d. **COMMENT:** At one level it may seem like the Court is saying Double M cannot use an agent or, in this case, the prime contractor, to take the necessary compliance actions for Double M.

(1) If the prime contractor was truly acting on behalf of Double M to comply with the statute, Double M would still be liable because it proceeded with its excavation before the statutory utility marking deadline had passed.

(2) Since the prime contractor was aware of the proper marking deadline, this would have been imputed to Double M, resulting in a violation of the Kansas One Call procedures.

(3) The Court, however, did not address these issues because Double M's basic defense was purely one of contractual delegation and did not raise agency issues.

4. **Court of Appeals gives "hold harmless" clause a liberal interpretation to require ex-husband to indemnify former wife for her criminal fraud penalties associated with defrauding the ex-husband's mother.** ***In re Marriage of Hudson***, 39 Kan. App.2d 417, 182 P.3d 25 (2008), *review denied* (Sept. 22, 2008).

   a. In the process of divorcing, William and Brenda entered into a separation agreement in which William was given control over the sale of a house with the proviso that: "Once the marital residence is sold, in the event a deficiency exists with regard to the second mortgage, Husband shall completely satisfy any such deficiency and hold wife harmless therefrom."

   b. The divorce was precipitated in part by Brenda's fraudulent procurement of $150,000 from William's mother to purchase the house.

   c. Brenda pled guilty to one count of federal wire fraud and was ordered, as part of her sentence, to make restitution to William's mother in the amount of $66,000. This amount represented the sum due after the house was sold and the first mortgage paid, which left $84,000 in sales proceeds that were paid to William's mother.

   d. Following the federal court's sentence requiring payment of the $66,000, Brenda sought a contempt order against William because he had failed to hold Brenda harmless for the $66,000, which also constituted the "deficiency" on the second mortgage held by William's mother.

   e. After finding that the "hold harmless" agreement "is the same as an indemnity agreement," the Court of Appeals concludes William must pay the $66,000 to his mother because it was encompassed by his indemnity agreement with Brenda.

      (1) In the process of arriving at its decision, the court states: "The rules governing the interpretation and construction of indemnity agreements are also the same as those relating to other types of contracts."

      (2) Although the court cites court of appeals and federal cases to support this proposition, it fails to acknowledge Kansas Supreme Court cases such as *Missouri Pacific R.R. Co. v. City of Topeka*, 213 Kan. 658, 518 P.2d 372 (1974), where it

is noted that "hold harmless" clauses, also referred to as an "exculpatory agreement," are construed strictly and limited to situations "plainly within the language used."

(3) Nor were cases such as *Hunter v. American Rentals, Inc.*, 189 Kan. 615, 371 P.2d 131 (1962), examined which hold that an indemnity clause relieving the indemnified party from obligations it owes to the public generally, or as defined by statute, is not enforceable.

(4) Instead, the court gives Brenda the benefit of the doubt by holding the restitution order was within the scope of the hold harmless clause and under the circumstances did not violate public policy.

(5) Dissenting Justice Malone, applying the factors set out in Restatement (Second) of Contracts § 178, believed the indemnity provision violated public policy when used to negate the sentence for restitution.

(a) **COMMENT:** Arguably the court could have arrived at the same conclusion applying existing Kansas law applicable to indemnity agreements. Indemnity is an area where the Kansas Supreme Court has been more demanding of the drafter to ensure the other party is fully apprised, at the time they enter into the contract, of the nature and scope of their indemnity obligation.

(b) **COMMENT:** In this case it appears pretty clear that since there was a mother/son relationship the parties would control the mother's demand for repayment by making the son liable through indemnity.

(i) It is doubtful the parties contemplated the indemnity would cover discharge of a sentencing condition in a federal criminal proceeding, even though it happened to be measured by the same deficiency amount.

(ii) This is the sort of situation where strict interpretation of the indemnity provision should limit it to the contemplated event: demand for repayment by the mother or her

assignee.

5. **COMMENT: Amendments to K.S.A. § 16-121, the Kansas anti-indemnity statute.** See **Appendix B** to this Outline for a complete copy of K.S.A. § 16-121.

a. Limiting freedom of contract over indemnity agreements seems to be a favorite topic of the Kansas Legislature; they now get a chance to address the issue every year.

b. In 2008 their focus resulted in significant amendments to K.S.A. § 16-121 which took effect on January 1, 2009.

c. As originally enacted in 2004 the statute prohibited, as being "against public policy," an "indemnification provision in a construction contract or other agreement . . . entered into in connection with a construction contract, which requires the indemnitor to indemnify the indemnitee for the indemnitee's negligence . . . ."

(1) Apparently one segment of the construction industry was losing in the bargaining process over who would be responsible for a party's negligence.

(2) In practice this determined who had to buy insurance to cover the risk. Since they couldn't win at the bargaining table, they turned to the Kansas Legislature.

(3) As with any situation where freedom of contract is ceded to a legislature, there will be unintended consequences. Having a legislature define the terms of a contract makes little sense unless it is acting to protect the general public, as opposed to stacking the deck for one commercial party against another.

d. After the enactment of K.S.A. § 16-121 there were other industries that rushed to try and have their contracts included in the prohibition on indemnity against negligence.

(1) This process caused these other industries to focus on the utility of indemnity agreements; utility they were seeking to voluntarily surrender to the legislature.

(2) Often a transaction will not take place unless certain risks can be allocated between the parties by contract.

(3) The indemnity against "negligence" is used to avoid having to litigate a negligence defense every time a party desires to enforce a contractual indemnity.

e. The 2008 amendments to 16-121 demonstrate four trends: first, certain industries want to make it clear certain activities *are not* encompassed by the law; second, certain segments of other industries want to make it clear their activities *are* encompassed by the law; third, the scope of the prohibition on certain indemnities is more fully defined to allow for greater, and lesser, coverage in listed situations; and fourth, certain indemnities are expressly excluded from the prohibition.

f. To decipher 16-121 there are ten definitions in § (a) that must be carefully read; the 2008 amendments add seven new definitions and extensively revise the prior definition of "construction contract" to expressly exclude listed activities at oil and gas well sites.

(1) The addition of the term "contract" expands coverage of the prohibition to "motor carrier transportation contract" and "dealer agreement or franchise agreement." Each of these new "contracts" are also the subject of their own extensive definitions.

(2) The definitions also distinguish between "mutual" and "unilateral" indemnity obligations.

g. The basic prohibition is found in § (b) which now applies to any "contract" which is defined to include "construction contract" and the additions noted above. Subsection (b) provides:

"An indemnification provision in a contract which requires the promisor to indemnify the promissee for the promissee's negligence or intended acts or omissions is against public policy and is void and unenforceable."

h. The amendment adds a prohibition on indemnity for any "intended acts or omissions."

(1) Does this mean that if the promissee takes action that is not negligent, but nevertheless "intentional," resulting in a loss to the venture, the promissee must alone bear the loss?

(2) This puts the party to a venture that is the "doer" or the "operator" at a distinct disadvantage. The passive party could set back, enjoy the benefits of the operator's actions, but force the active party to shoulder all the risk, and therefore loss, under their contract.

i. Subsection (c) expands the indemnity prohibition to insurance coverage by providing:

"A provision in a contract which requires a party to provide liability coverage to another party, as an additional insured, for such other party's own negligence or intentional acts or omissions is against public policy and is void and unenforceable."

This provision takes away from the parties the flexibility of placing the burden of insurance on the party who may be best able to insure the risk.

j. Recognizing that indemnity agreements can serve a useful purpose in some situations, subsection (d) was added to specifically exempt certain transactions from the prohibition.

(1) Exemptions include: a contractor's agreement to provide "general liability insurance;" indemnification of a contractor against "strict liability under environmental laws;" indemnification as part of certain settlement agreements; insurance contracts and bonds issued by "an insurer or bonding company;" and certain indemnity agreements which "will be supported by liability insurance coverage to be furnished by the promisor" subject to specific limitations.

(2) The broadest exemption, however, is found at § (d)(5) and includes:

"(5) a separately negotiated provision or provisions whereby the parties mutually agree to a reasonable allocation of risk, if each such provision is: (A) Based on generally accepted industry loss experience; and (B) supported by adequate consideration; . . . ."

(a) Subsection (5) has the potential to negate the 16-121 prohibition when the provision is "separately negotiated."

(b) This is an invitation for the party drafting the agreement to ensure the indemnity clause receives the appropriate attention by being conspicuous and containing recitations regarding allocation of risk and the industry context for the allocation.

(c) The "adequate consideration" requirement should be satisfied by the underlying deal that prompted the parties to contract with one another. It is possible, however, that "adequate" consideration is being used as a statutory equity to allow courts to limit the effect of the indemnity even though all "contract" consideration requirements have been met.

k. To avoid using choice of forum and choice of law to circumvent the indemnity prohibition, subsection (e) provides:

"Notwithstanding any contractual provision to the contrary, the laws of the state of Kansas shall apply to and govern every contract to be performed in this state. Any litigation, arbitration or other dispute resolution proceeding arising from such contract shall be conducted in this state. Any provision, covenant or clause in such contract that conflicts with the provisions of this subsection shall be void and unenforceable."

(1) An immediate question is whether Kansas law must be applied only to the extent necessary to give effect to 16-121, or whether any contract which has an indemnity provision must apply Kansas law, in a Kansas forum, as to all issues.

(2) For example, could a party to a construction contract subject to 16-121 agree not to enforce the indemnity provision but still litigate contractual performance issues in a forum outside of Kansas?

(3) Under similar facts, would they be compelled to apply Kansas law to the non-indemnity issues?

(4) Could a party to the contract allege it contains language that is tantamount to an indemnity so as to compel application of Kansas law in a Kansas forum?

l. Although there are no reported appellate cases regarding K.S.A. § 16-

121, I predict the statute will be widely used to try and negate allocations of risk within contracts and to negate choice of law and choice of forum clauses that would otherwise be enforceable absent 16-121.

(1) It will become a litigation tool to try and avoid contractual provisions that have proven very useful and beneficial in making deals work that might otherwise fail.

(2) It is an example of legislation to address matters that are best left to the market place where commercial parties can adjust to the realities of the industry in which they operate.

## B. Performance and Breach

### 1. Member's expulsion from private country club for violating club rules is a matter of contract and the contract was not breached in this case. *Pollock v. Crestview County Club Association*, ___ Kan. App.2d ___, 205 P.3d 1283 (May 1, 2009).

a. Pollack joined Crestview in the early 1980's. He had previously received written censures in 1992 and 1995 for loud and offensive language and was warned that such behavior could result in expulsion.

b. March 8, 2006 he called another member, the club's former president, "a condescending asshole . . . ." A member who heard the comment filed a complaint about Pollack's conduct.

c. Under the club's bylaws the board has a number of options with how it deals with bad behavior, including expulsion. Pollack was notified that a complaint had been made, that an investigation was being conducted, and that Pollack could provide whatever information he desired for the board's consideration. Pollack responded through his attorney. The board met, and by a three-fourths affirmative vote required by the bylaws, expelled Pollack as a club member.

d. Pollack sued the club asserting violation of his due process rights and a breach of contract. The trial court held for the club; the Court of Appeals affirms.

e. Due process claim:

(1) Due process, in a constitutional context, is a protection against state action.

(2) Because there is no state action with regard to the club's actions, there can be no constitutional due process claim.

(3) The "due process" arguments in this context are really contract arguments: Pollack asserts he was not given the process he was due under the club's bylaws.

f. Contract claim:

(1) "'The relationship between a social club and its members is one of contract.' . . . The rules, regulations, and bylaws of social clubs generally establish the terms of such contracts."

(2) "The 'bylaws, and rules of private organizations create a legally enforceable agreement in the nature of a contract between the organization and the member because of corresponding mutual obligations – by the member to follow the rules of the organization, and by the organization to fairly apply those rules.'"

(3) "Courts generally defer to social clubs on questions whether a member exhibits appropriate conduct at the club."

(4) "[C]ourts generally defer to social clubs in matters of membership discipline provided there is substantial compliance with the social club's bylaws."

(5) Court rejects arguments that the proper procedures were not followed.

(6) What is unacceptable conduct is a "'matter of internal government and discipline of the order and is for its final determination.' . . . Following our Supreme Court's guidance, we will not decide whether Pollock's conduct was acceptable behavior in the Men's Grill."

2. **Buyer's action in failing to give seller notice of default and an opportunity to cure constituted a breach of contract.** ***Inter-Americas Insurance Corporation v. Imaging Solutions Company***, 39 Kan. App.2d 875, 185 P.3d 963 (2008).

   a. Inter-Americas Insurance Corporation entered into a contract with Image Solutions Company to have Image develop software, provide hardware to run the software, install the system, and provide support services to Inter-Americas' employees.

      (1) Image delivered most of the contracted items, and Inter-Americas' paid $213,904.31 then due under the contract.

      (2) However, there were still things Image needed to do to fulfill its contract and get the system up and running in accordance with their contract.

      (3) Despite several attempts by Image to complete the contract, Inter-Americas, without prior complaint or notice, informed Image on October 5, 2005 it had breached their contract and demanded $225,405.88 in damages.

      (4) When Image failed to pay the demanded money Inter-Americas filed suit on January 5, 2006.

   b. The trial court granted summary judgment to Image finding that any delay in performance was caused by Inter-Americas and it was Inter-Americas, not Image, that breached the contract by failing to give Image a reasonable opportunity to perform.

   c. The Court of Appeals affirms the trial court's holding that Inter-Americas was the breaching party but reverses and remands so the trial court can determine Image's recoverable damages.

   d. What body of contract law applies to this problem?

      (1) The court first finds that this mixed goods and services contract is governed by Article 2 of the UCC as a "sale of goods."

      (2) Applying Kansas precedent, a sale of computer software is a sale of "goods" and in this case, where $35,000 of the $240,000 contract were services, the services were incidental

to the sale of goods.

(3) **COMMENT:** Although not mentioned by name, the court applies the "predominant factor" test to conclude that since this contract is predominantly a sale of goods as opposed to services, Article 2 of the UCC will apply to all of the contract provisions, whether pertaining to goods or services. See *Care Display, Inc. v. Didde-Glasser, Inc.*, 225 Kan. 232, 589 P.2d 599 (1979) (applying predominant factor test to determine contract was primarily for services and therefore not subject to the UCC statute of frauds for a sale of goods).

e. Because the contract did not specify a time-line for performance, Image was obligated to perform its contract duties within a "reasonable time" as required by K.S.A. § 84-2-309(1).

(1) Under K.S.A. § 84-1-204(2) "reasonable time" for taking any action depends on the nature, purpose, and circumstances of the required action.

(2) The uncontroverted facts indicated that Image performed within a reasonable time and therefore did not breach the contract.

f. Image counterclaimed for breach of contract against Inter-Americas for its actions in preventing Image's performance. Image also asserted Inter-Americas was in breach for failing to give Image notice of the alleged breach and a reasonable time to cure any breach.

(1) Affirming the trial court's grant of summary judgment on Image's counterclaim, the court of appeals notes the UCC imposes a duty on Inter-American to give "seasonable" notice of any claimed breach and an opportunity to cure.

(2) As the court notes: "[I]f Inter-Americas believed ISC [Image] was in breach of the contract, under the UCC it had a duty to tell ISC of its breach." *Id.* at 887, 185 P.3d at 970.

(a) For this proposition the court refers to K.S.A. § 84-2-602(1) dealing with "rejection of goods," which requires that: "Rejection of goods must be within a reasonable time after their delivery or tender.

(b) It is ineffective unless the buyer seasonably notifies the seller." *Id.* Under K.S.A. § 84-1-204(3) "seasonable" is within the time agreed or within a reasonable time.

(3) Regarding the opportunity to cure, the court quotes K.S.A. § 84-2-508 and then observes that § 84-2-508: "allows ISC [Image] the right to cure any claimed breach if it could do so within the time for performance under the contract or within a reasonable time if it had reasonable grounds to believe that Inter-Americas was satisfied with its performance."

(a) The right to cure under UCC § 2-508 has created some interesting interpretive issues.

(b) The buyer's duty to give notice of "rejection," and the seller's ability to cure a defect in performance, are on-going obligations and rights for contracts that contemplate a series of performances.

(c) **COMMENT:** Note how this on-going process is further expanded when you mix goods and services. The goods may be delivered in a one-shot deal, followed by a long-term set of performances related to the "service" component of the transaction.

g. Good faith issues. In the course of its opinion the court also notes that "'Kansas courts imply a duty of good faith and fair dealing in every contract.'"

(1) **COMMENT:** Although the court states this rule, it fails to discuss how it applies to the facts of this case.

(2) The concept can be applied in at least two contexts: performance and enforcement.

(3) Good faith *performance.*

(a) First, where one party is dependent upon the other in order for performance to take place, the parties must cooperate to allow performance to go forward.

(b) In this case, Inter-Americas must cooperate with

Image to the extent Image can have access to Inter-Americas facilities and personnel so it can perform its contracted duties.

(c) Although this was not specified in the parties' contract, it is clearly implied that the parties would do whatever is necessary to allow for performance, as contemplated by the contract, to take place.

(4) Good faith *enforcement*. If a party does not believe the other party is acting in accordance with the contract, it is implied, absent express language addressing the matter, that they will let the party know about the problem so they can correct their nonperformance.

(5) **COMMENT:** Technically, it is not correct to say these obligations are "implied" in the UCC context because K.S.A. § 84-1-304 provides a *statutory* basis for good faith stating: "Every contract or duty within the UCC imposes an obligation of good faith in its *performance and enforcement*." (Emphasis added).

(6) **COMMENT:** Although the statutory obligation of good faith cannot be negated by a blanket disclaimer, it can be limited through express terms that provide precise direction on the matter at issue.

(a) This is provided for in K.S.A. § 84-1-302(b) which states, in part: "The parties, by agreement, may determine the standards by which the performance of those [good faith] obligations is to be measured if those standards are not manifestly unreasonable."

(b) This allows the parties to exercise their freedom of contract to specify their obligations, which will be enforced, as stated, so long as they are not unconscionable.

(c) In a commercial setting, where unconscionability is almost impossible to establish, it permits the parties to settle these matters through negotiation and agreement with the statutory good faith obligation being triggered only in those situations where the parties

have not fully expressed their agreement.

(7) For non-goods situations, the common law, as restated by the RESTATEMENT (SECOND) OF CONTRACTS § 205, provides by implication that: "Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement." The development of the law in this non-goods setting has tracked closely that under Article 2 of the UCC.

3. **Demand must be made to be eligible for cancellation as a remedy for oil and gas lessee's failure to develop "deep rights" under Kansas' "Deep Horizons" Act.** ***Lewis v. Kansas Production Company, Inc.***, 40 Kan. App.2d 1123, 199 P.3d 180 (2009).

a. 1972: oil and gas lease granted by landowner; production obtained from the leased land and production continues from the land.

b. 1994: the owner of the oil and gas lease divided the leasehold interest by depth with one portion covering formations from the surface to the base of the then producing formation (the "shallow" rights); and another portion covering formations below the base of the producing formation (the "deep" rights).

d. 2004: the Lowes, who were selling the land to Lewis, sent Kansas Production Co. (KPC) a demand to file a release of its deep rights under the oil and gas lease. This was not a demand for development, but rather a demand, pursuant to K.S.A. § 55-201 (the Kansas procedure for demanding release of expired or terminated oil and gas leases), that KPC clear the landowner's title of its lease rights because its lease had terminated.

e. KPC is the successor to the deep rights. Lewis acquired the surface and the lessors' rights in the oil and gas lease in 2005. No effort has been made to develop the deep rights.

f. The Kansas Legislature, in 1983, enacted what has become known as the Kansas "Deep Horizons" Act (K.S.A. §§ 55-223 to 55-229 (2005)), to assist landowners in obtaining exploration and development of portions of leased lands, held by production, that lie below "the base of the deepest producing formation as of the date of such action." K.S.A. § 55-227.

(1) The Act creates a presumption that "the lessee has breached

and violated such [implied or expressed] covenant [of reasonable exploration or of reasonable development] insofar as it relates to such subsurface part or parts of land" when the lessor presents evidence:

(a) There is currently no mineral production from the deeper horizons; and

(b) "[I]nitial oil, gas or other mineral production on the lease commenced at least 15 years prior to the commencement of such action . . . ." K.S.A. § 55-224.

(2) The Act is designed to place the burden of proof on the lessee to justify its failure to develop the deeper horizons once 15 years has passed since the last new production ("initial" or "other") from the leased land.

g. The trial court held that KPC violated the deep horizons act by failing to timely explore or develop its portion of the lease and that pursuant to K.S.A. § 55-226 the trial court could order the remedy of cancellation.

h. The issue on appeal is whether cancellation could be ordered when the lessor fails to make any prior demand *for further exploration or development*. KPC argues the remedy should have been conditional cancellation.

i. K.S.A. § 55-226 states:

> "If the court determines that the lessee has failed to comply with such covenant, the court may grant the lessee a reasonable time in which to comply, *or the court may issue an order terminating the lessee's right to such subsurface part or parts as are the subject of such action*. The court may enter such other orders as the interests of the parties and equity may require." (Emphasis added).

j. At common law, Kansas courts have equated "cancellation" with a "forfeiture" which should be avoided unless the landowner lacks any other adequate remedy, such as damages.

(1) The common law has also established that the lessee is

entitled to notice and an opportunity to cure any alleged breach of an implied covenant.

(2) Therefore, it is generally held in Kansas that for a lessor to be eligible for the remedy of outright cancellation of rights under a lease for failure to further develop or explore, the lessor must first demand compliance with the covenant, and provide the lessee with a reasonable opportunity to respond to the demand.

k. The Court of Appeals reverses the trial court focusing on another section of the Deep Horizons Act which states:

> "This act shall not alter or affect substantive rights or remedies under any such mineral leases under the common law or statutes of the state of Kansas. The evidentiary presumption afforded by this act shall be cumulative and in addition to all other substantive rights and remedies in existence under the common law and statutes of this state on the effective date of this act." K.S.A. § 55-229.

(1) The Court of Appeals finds: "K.S.A. 55-229 indicates that K.S.A. 55-226 is merely a codification of the preexisting common-law remedy of cancellation with all of its common-law requirements."

(2) The court then concludes, holding:

> "Since there has been no compliance request, and no evidence of abandonment or futility in requesting compliance, cancellation is not appropriate. KPC's actions have been sluggish, but before the extreme remedy of forfeiture could be imposed, under these facts, there should have been a demand for compliance. Absent such a demand, under these facts, KPC should be given a reasonable time to comply with the lease."

l. **COMMENT:** In Kansas, because an oil and gas lease is classified as a *profit à prendre*, rights under an oil and gas lease can be abandoned.

(1) Abandonment is a totally different concept from an implied

covenant. Abandonment is a *property* concept that applies when an owner has the intent to abandon their property. The "intent to abandon" is the critical inquiry.

(2) Although the Court of Appeals in *Lewis* is momentarily confused by the relationship between abandonment and an implied covenant, this confusion is caused by the Kansas Supreme Court's strained analysis in *Rook v. James E. Russell Petroleum, Inc.*, 679 P.2d 158 (Kan. 1984). In *Rook* the Court gratuitously imputes an intent-to-abandon to the non-developing lessee.

m. **COMMENT:** Breach of an implied covenant is a purely contractual analysis which requires that:

(1) The obligation be defined (applying the "prudent operator" analysis);

(2) the lessee's actions compared to the obligation; and

(3) a determination made whether there is a breach.

(4) Once a breach is found to exist, as in this case, the issue is still one of determining the appropriate *contract* damages.

(5) The opinion in *Lewis* is consistent with a proper *contract* analysis of the issue; even though the court must first apply the statutory presumption created by the Deep Horizons Act to determine whether the lease contract has been breached.

## III. PROPERTY LAW

### A. Adverse Possession, Prescriptive Easements, Implied Easements

**1. Agreement with prior landowner regarding fence location, followed by over 15 years of maintenance, gave the County ownership of the land on its side of the fence through adverse possession.** ***Chesbro v. Board of Douglas County Commission***, 39 Kan. App.2d 954, 186 P.3d 829 (2008), *review denied* (Sept. 24, 2008).

a. In 1972 Fishburn approached the County about building a fence between his property and County property. The parties agreed on the placement of the fence, which placed about 10 feet of Fishburn's land on the County-side of the fence. The resulting 10-foot strip consisted of a large ditch. The parties split the cost of the fence and the County maintained the ditch area by periodic mowing and weed spraying.

b. In 2004 Chesbro purchased the land from Fishburn and sought an access permit onto a County road adjacent to the 10-foot strip of land. The County denied the permit because Chesbro did not own land abutting the County road. Chesbro asserted he owned the 10-foot strip of land and therefore should have been granted an access permit.

c. The trial court held the County had obtained ownership of the 10-foot strip by adverse possession.

d. The warranty deed from Fishburn to Chesbro described the original tract of land which ran to the County road. The County did not have anything of record to indicate it was claiming the 10-foot strip.

e. The Court of Appeals affirms the trial court's finding of adverse possession, noting:

(1) K.S.A. § 60-503 states: "No action shall be maintained against any person for the recovery of real property who has been in open, exclusive and continuous possession of such real property, either under a claim knowingly adverse or under a belief of ownership, for a period of fifteen (15) years."

(2) Under 60-503 adverse possession can be obtained either under a claim "knowingly adverse" (meaning a "hostile" holding) or a non-hostile holding through a "belief of ownership."

(a) The court notes: "The County's belief of ownership must have been in good faith and reasonable under all the facts and circumstances." Quoting a 1972 Kansas Supreme Court case.

(b) Think so? If it is in "bad faith," couldn't we then call it "hostile" and "knowingly adverse" to the other party?

(c) Is it possible to have a situation that is a bad faith belief of ownership that is not then knowingly adverse? Doubtful.

(d) The amendment to 60-503 was intended to avoid the hostile/non-hostile trap. The "good faith" gloss would seem to be unnecessary – but is nevertheless part of the current Kansas law.

(3) The County claimed adverse possession relying upon its good faith belief in ownership of the 10-foot strip.

(4) The County's possession was "open, continuous and exclusive" considering the nature of the land and the sort of activity you would expect an owner to conduct on the land. In this case the land was a road ditch and the County's actions were consistent with maintenance of a road ditch.

(5) The change in ownership would not interrupt the statute. "Tacking" applies to the rightful owner as well as the adverse possessor. In this case it really didn't matter because the County already had the requisite 15-years of open, continuous and exclusive possession under a belief of ownership long before the property was transferred to Chesbro.

f. Statements or actions by County personnel after adverse possession has been obtained will not cause the County to lose title.

g. County need not file anything of record to obtain ownership through adverse possession. "A claim of adverse possession does not require possession under a deed or other muniment of title."

h. The County's decision to deny Chesbro's access permit was proper because Chesbro did not own property abutting the road.

2. **Court holds pipeline company obtained prescriptive easement even though pipeline held an unrecorded express easement.** ***Southern Star Central Gas Pipeline, Inc. v. Greuel***, Case No. 08-2115-KHV, 2009 WL 1208065 (April 30, 2009).

   a. In 1917 the landowner granted Wichita Pipe Line Company an easement to construct and maintain oil and gas pipelines on the land. The land burdened by the easement was ultimately conveyed to Greuel in 2007. Southern Star ultimately became the owner of the Wichita Pipe Line easement.

      (1) The only problem was the pipeline easement had never been recorded and Greuel apparently qualified as a bona fide purchaser without notice of the unrecorded easement.

      (2) It would appear Greuel would take the property unburdened by the unrecorded easement.

      (3) The court finds: "Because the original easement was not recorded until after the Greuels purchased the property, they did take the property free of the original express easement and neither side claims otherwise. See K.S.A. § 58-2223 (unrecorded instruments not enforceable unless party has notice thereof)."

   b. Southern Star asserts it has acquired an easement to use the property for pipeline construction and maintenance by prescription.

      (1) "Southern Star argues, however, that as a matter of law it owned a prescriptive easement across the property beginning in 1973, if not before, and that the Greuels' lack of knowledge is irrelevant."

      (2) "Southern Star specifically contends that it began entering the property as early as 1958, began transporting gas through the pipeline in 1962 and continued to access the easement until 1973 when its prescriptive rights attached."

      (3) **NOTE:** A most interesting inquiry would be under what authority did Southern Star enter the property in 1958 and use the pipeline until 1973, and up to the present? The answer would be the 1917 express easement granting ***permission*** to use the land to construct and maintain its pipeline.

c. The court agrees with Southern Star finding:

(1) Kansas applies the adverse possession statute, K.S.A. § 60-503, to determine the existence of a prescriptive easement.

(2) There was open possession of the property and prior owners acknowledged its right to possession.

(3) Possession of the easement was exclusive.

(4) Use was continuous.

(5) Southern Star had a good faith "belief in ownership."

(a) The court notes: "Good faith belief of ownership cannot be established where the party claiming the easement was accessing the property with the permission of the property owner."

(b) "Stated another way, a license granting access to land cannot ripen into a prescriptive easement because use of the land under the license is permissive and not under a good faith belief of ownership."

(c) **COMMENT:** Then how can Southern Star possibly have a prescriptive easement when its original entry and use was pursuant to an express easement?

(d) Counsel for the Greuels raised the permissive use issue: "The Greuels . . . argue that Southern Star accessed the property with the permission of the landowner because it gave value for the 1917 easement and paid the Greuels' predecessors for access to the land between 1917 and 1984."

(i) Although the court states Southern Star's rebuttal argument to this claim, the court does not address it but states: "Southern Star's conduct was entirely consistent with the un-recorded express easement."

(ii) That should mean Southern Star loses because its actions were consistent with the permission

it had been expressly granted in 1917. But, the court concludes Southern Star had established the belief in ownership required by 60-503.

(6) Southern Star satisfied the required 15-year period; here it was on the property from 1958 to 2007, 49 years.

d. I think the facts clearly indicate that Southern Star was engaged in a permissive use of the property until 2007. The prescriptive easement clock began in 2007 when Greuel asserted the easement was not effective. At that time Southern Star's possession became "adverse" ("hostile" or "belief of ownership"). Southern Star is about 14 years shy of a prescriptive easement.

e. **THE COMMENTATORS:** "To say that possession is hostile should mean nothing more than that it is without permission of the one legally empowered to give permission, usually the owner. ***Any kind of permissive use, as by a*** tenant, licensee, contract purchaser in possession, or ***easement holder is rightful, not hostile.***" WILLIAM B. STOEBUCK & DALE A. WHITMAN, THE LAW OF PROPERTY 453, 856 (applying same concepts of permissive use for prescriptive easements to adverse possession) (3d ed. 2000) (emphasis added).

3. **Scope of implied easement to use road to access farmland included easement to access house on land and to run utilities to serve a house on the land.** ***Stroda v. Joice Holdings, LLC***, Case No. 100,733, 2009 WL 1347241 (Kan., May 15, 2009).

a. 1952 Stroda's predecessors purchased farmland containing an occupied residence in the NW1/4. They were allowed an implied easement across the neighboring SW1/4 to access their land. 1957 the Stroda predecessors acquired the SW1/4 which merged their easement out of existence.

b. 1985 through inheritance Marie became owner of the SW1/4 and brother Edmond the NW1/4. Edmond was allowed an implied easement across the SW1/4 to access the NW1/4. Plaintiff Ed Stroda became owner of the NW1/4; in 2003 the SW1/4 was acquired by the defendant Joice Holdings.

c. 2006 Stroda sought to sell the NW1/4 for use as a single residence and claimed the implied easement across the SW1/4 would support

not only access to the NW1/4 for agricultural purposes but also to access a residence and to provide utility service to the residence. Joice Holdings asserted the scope of the implied easement was limited to agricultural use.

d. The existing residence on the NW1/4 had ceased being occupied by 1957 but the prior residential use was apparent from what was remaining on the land.

e. Trial court: Storda entitled to an implied easement that allows access for agricultural use and to access a single residence, including the laying of utilities to the residence within the confines of the existing road easement.

f. Rules applicable to interpretation of express easements and prescriptive easements are not to be applied to implied easements. The court states:

"Express easements and prescriptive easements contain fundamental differences from those that are implied. The scope of an express easement is much more ascertainable; one essentially looks at the language employed by the parties. . . . By contrast, an implied easement obviously has no express language and external evidence of intent becomes much more important. While we acknowledge that a prescriptive easement is similar to an implied easement in that neither has express language to interpret for determining the intent of the parties, prescriptive easements are interpreted narrowly because they are created by the adverse use of the property, with the use during the prescriptive period defining the scope of the easement."

g. The court concludes that here: "Accessing a single residence is within the scope of the implied easement." Although the court refers to a number of concepts to arrive at its conclusion, the following appeared to be important:

(1) Although the NW1/4 at all relevant times was not being used for residential purposes, there was evidence on the land that a residence once existed on the land.

(2) Quoting from the RESTATEMENT (FIRST) OF PROPERTY § 484, comment b:

"Yet it does not follow that the use authorized is to be limited

to such use as was required by the dominant tenement at that time [i.e. access for agricultural development]. It is to be measured rather by such uses as the parties might reasonably have expected from the future uses of the dominant tenement [i.e., past use as a single residence]. What the parties might reasonably have expected is to be ascertained from the circumstances existing at the time of the conveyance. It is to be assumed that they anticipated such uses as might reasonably be required for a normal development of the dominant tenement [i.e. a single residence in conjunction with the farm]. It is not to be assumed, however, that they anticipated an abnormal development [i.e. residential subdivision or multiple houses]."

h. Applying the same analysis, the court concludes that access for utilities to serve a single residence on the property is also within the scope of the easement.

(1) "We observe that even when the use is reasonable, it must be necessary; the level of necessity required has been found to be less than strict necessity, but more than inconvenience."

(2) "In our view, a lack of utilities to a new house in Kansas goes beyond mere inconvenience and begins to approach the unlivable."

(3) "A house generally is not considered to be a residence without water, electricity, and similar utilities, *e.g.*, the ability to be heated and cooled, lit in the dark, and equipped for communication with the outside world."

i. In closing, the Court acknowledges the RESTATEMENT (THIRD) OF PROPERTY: SERVITUDES by observing: "We find nothing in the current incarnation of the Restatement of Property that changes our analysis of these two issues."

4. **Proper remedy when pipeline placed on land without an easement: dig it up and get it off there!** ***Friess v. Quest Cherokee, L.L.C.***, Case No. 100,050, 2009 WL 1563365 (Kan. Ct. App., June 5, 2009).

a. Quest's contractor was negotiating with the beneficiary of a trust, Steven Friess, in an effort to obtain an easement to allow Quest to construct, operate, and maintain a pipeline across land owned by the

Friess Trust. Negotiations were never successful but Quest's contractor sent a check to the Friess Trust, which was never accepted. Nevertheless, without an agreement on the easement, or other consent or authorization,Quest placed its pipeline on the Trust's property. When it was discovered, the Trust demanded $100,000 for an easement. Quest refused and the Trust sued seeking a mandatory injunction to force Quest to remove its pipeline from the Trust's land.

b. The trial court granted the mandatory injunction.

c. The Court of Appeals affirms the trial court noting:

(1) The Friess Trust did not have an adequate remedy at law:

(a) "The construction on landowner's property of any structure without any easement agreement has been recognized as a continuing violation of the landowner's rights that does not cease with the completion of the structure and generally cannot be compensated by monetary damages."

(b) "This principle is consistent with the general principle that legal remedies are inadequate to redress ongoing or continuing violations."

(2) The trial court was not required to "balance the equities":

(a) Essentially there are no equities to balance.

(b) This was not an innocent act by Quest, but rather a "foolish or negligent" act.

(c) Quest had no authority nor any reasonable basis for believing it had been granted authority to install the pipeline.

(d) "Moreover, we find it incredulous that a company in the pipeline business would think it innocent conduct to proceed to construct a line on another's land based solely on an 'agent's consent' and without a written easement agreement."

(i) The trial court had found that Steven Friess,

who Quest's contractor dealt with at all times, did not have either express or implied authority to grant consent for the pipeline construction. He was merely a beneficiary under the trust.

(ii) The Court of Appeals avoids the agency issue by noting even if they thought they had some sort of agreement with an agent, it still would have been unreasonable to proceed without a written easement.

d. What does Quest do now? Unless its pipeline can qualify for condemnation as a common carrier, Quest will have to convince the Trust to sell it an easement or move the pipeline. Absent a condemnation remedy, the price of any easement will probably be just a little less than the cost of removing the pipeline.

## B. Conveyances

### 1. Conveyance of "All coal . . . together with the right to mine and remove same" Does Not Include Methane Gas Contained Within the Coal. *Central Natural Resources, Inc. v. Davis Operating Company*, 288 Kan. 234, 201 P.3d 680 (2009).

a. 1924: Landowners in Southeast Kansas conveyed "all coal . . . together with the right to mine and remove same" to Central Natural Resources, Inc.

b. 2004: two oil and gas developers obtained oil and gas leases from the landowners, drilled into the coal seams beneath their land, and began producing methane gas from the coal.

c. When Central discovered that its coal had been entered without its authorization, it brought suit for trespass, conversion, and to quiet title to its coal and the methane gas within its coal.

(1) The trial court held that Central did not own the methane within the coal and the parties were permitted to pursue an interlocutory appeal focusing solely on the methane ownership issue.

(2) The Kansas Supreme Court affirms the trial court holding that

the conveyance of "coal" does not encompass methane within the coal.

d. Noting that methane was viewed as a hazardous waste material at the time of the conveyances, the Court finds it would be unreasonable to think the coal owner intended to obtain rights to the methane within the coal.

e. Central argued that just the opposite conclusion should be drawn from the well-known hazards associated with methane because, at the time of the conveyances:

(1) Central, as the mine operator, was required by statute to manage the methane by destroying it through ventilation;

(2) coal in Southeast Kansas was known to contain methane and known to require special attention as part of the deep mining process;

(3) the coal grantee had employees killed and injured by methane in its other Southeast Kansas coal mines;

(4) and it was generally known that gas was a hazard and problem in Southeast Kansas coal mines.

Central argued that with this background, the parties would have intended that the methane within the coal would have been included in a grant of "all coal . . . together with the right to mine and remove same . . . ."

f. Central also argued that when applying K.S.A. § 58-2202 to the conveyance, all doubts regarding the scope of the conveyance should be resolved against the grantor and in Central's favor, as the grantee.

(1) K.S.A. § 58-2202 states, in part: "[E]very conveyance of real estate shall pass all the estate of the grantor therein, unless the intent to pass a less estate shall expressly appear or be necessarily implied in the terms of the grant."

(2) Central argued that if the grantors desired to retain the methane within the "coal" it conveyed, the burden was on the grantors to clearly express their intent in that regard.

(3) The Court rejects this argument by first holding that K.S.A. § 58-2202 cannot apply to this sort of conveyance because it conveys something less than the entire fee in the property.

(a) Apparently K.S.A. § 58-2202 can no longer be used in situations where the conveyance is of something less than the entire fee.

(b) This brings into question prior Kansas Supreme Court analysis where the statute was considered in interpreting conveyances of "minerals."

(4) As an alternative ground for decision, the Court states that even if the statute did apply to this conveyance, it still would not assist Central because the grant of "coal" does not suggest the grant of "methane."

g. **COMMENT:** The Court was heavily influenced by the U.S. Supreme Court's analysis and conclusion in *Amoco Production Co. v. Southern Ute Indian Tribe* and, by negating the potential effect of K.S.A. § 58-2202, achieves almost a "matter of law" approach to what would otherwise be a factual inquiry.

(1) It appears title examiners in Kansas can now safely conclude that a grant of "coal" will not include the methane within the coal, unless the grant expressly addresses methane ownership and gives it to the coal owner.

(2) **NOTE:** I was one of the co-counsel for Central. At the time of this writing, the trespass issues remain to be resolved in the trial court.

2. **Deeds were properly delivered prior to donor's death.** ***Johannes v. Idol,*** 39 Kan. App.2d 595, 181 P.3d 574 (2008).

a. Issue: Were deeds of land properly delivered prior to the grantor's death so the lands belonged to the grantees and were not part of the grantor's estate?

b. The donor/grantor, Margret Johannes died unmarried, without children, and intestate in 1989.

c. This dispute concerns four tracts of land conveyed to three donees,

Gertrude Reader, Hazel Denison, and Isabel Idol (three of Margret's four sisters, she also had four brothers).

d. The conveyances were gifts from Margret to Gertrude, Hazel, and Isabel, made by deeds signed sometime in 1967.

(1) Each deed contained the following reservation of a life estate in Margret:

"Reserving unto party of the first part [Margret] and her assigns the full benefit, use, rents, issues and profits from the above described real estate, for and during her natural life."

(2) "Margret signed the deeds and had them notarized. However, the acknowledgment and the notary's signature do not include the day or month that the deeds were acknowledged."

(3) "According to both Hazel and Isabel, Margret delivered the deeds to them in 1967 or 1968. Isabel placed the deeds in a safety deposit box she owned with Hazel. Margret's name was not on this safety deposit box."

e. Court affirms trial court's grant of summary judgment finding that the deeds had been properly delivered to Hazel, Isabel, and Gertrude prior to Margret's death and therefore they became the owners in fee of their respective tracts of land at Margret's death.

f. Legal principles applied by the courts to resolve the issue:[1]

(1) "[T]o transfer title through a warranty deed, the grantor must cause the deed to be delivered to the grantee during the grantor's lifetime."

(2) "Delivery may me constructive as well as actual or personal, and it may be made to a third party [*e.g.* the deed to Gertrude given to Hazel and Isabel] to hold for the grantee, where an intention is manifested to give the conveyance present effect."

(3) Delivery is a question of intent to be determined by

[1]The Court of Appeals reproduces major potions of Brown County District Court Judge James A. Patton's opinion which is both a concise but comprehensive, effective statement and application of the law in this area.

examining all the facts and circumstances surrounding the transaction to ascertain whether "the grantor had a present intent to divest himself or herself of title to the property and vest it in the grantee."

(4) "Because delivery is a question of intent, it is normally a question of fact. However, when the facts are not controverted, then delivery is a question of law."

(5) "The rule of law is that in deed of gifts to children or relatives, the reservation by the grantor of the use of the property during his lifetime is evidence of an intention to deliver the instrument before his death, for there could be no purpose in placing such a reservation in the deed if it were not delivered in his lifetime."

(6) "When a deed that is duly executed and acknowledged is found in the grantee's possession, in a third-party's possession, or when the deed has been recorded, it is presumed that the grantor delivered the deed."

(7) "Conversely, when a deed is signed and acknowledged but found in the grantor's possession, the law presumes that the grantor did not deliver the deed."

(8) "The party challenging the preceding presumptions must supply clear and convincing evidence to rebut the presumption."

(9) "Recording is not necessary to effectively deliver a deed . . . ."

g. Summary Judgment Proper? Although delivery based upon the oral testimony of Hazel and Isabel, the plaintiffs had the burden to come forward with evidence to controvert their statements.

(1) "[A]n unsupported challenge to a witness' credibility is not sufficient to create a genuine issue of a material fact."

(2) "[T]he failure of appellants to provide affirmative evidence, contrary testimony, or a writing that challenges Hazel's or Isabel's statements concerning actual delivery of the deeds to them clearly justifies the district court's ruling granting partial

summary judgment that valid delivery of the deeds occurred."

3. **Delivery of transfer-on-death deed is not required but recording is mandatory.**

   a. Today, when tax planning is not an issue, it is possible to use a "transfer-on-death" deed to provide for a conveyance of land that does not take effect until the death of the grantor. Until the grantor dies, they can change the grant, dispose of the property to others, or encumber the property in any way.

   b. K.S.A. §§ 59-3501 to 59-3507 (2005).

   c. Although the statutes allow the grantor to avoid all the traditional delivery requirements (the grantee need not even be aware of the conveyance), it imposes a new mandatory requirement: "acknowledging and recording in the office of the register of deeds in the county where the real estate is located, prior to the death of the owner . . . ." K.S.A. § 59-3502 (2005).

   d. If the transfer-on-death deed is properly created, it "shall not be considered a testamentary disposition and shall not be invalidated due to nonconformity with the provisions of chapter 59 of the Kansas Statutes Annotated." K.S.A. § 59-3507 (2005).

      (1) In this manner, the grantor can avoid creating a present interest in the grantee, but still have it qualify as a gift if it remains unrevoked at the donor/grantor's death.

      (2) Nor will it violate the statute of wills for failing to comply with the formalities of a will.

   e. Similar provisions for "motor vehicles." K.S.A. §§ 59-3508 to 59-3512 (2005).

   f. These provisions regarding real estate and automobiles complete the range of property that can be transferred outside of probate – but without the undesirable aspects of joint tenancy.

      (1) Provides the same sort of benefits that have been available under "pay-on-death" bank accounts.

      (2) Avoids issues of current ownership, percentage of ownership,

contribution by the parties, and creditor rights.

g. K.S.A. § 59-3513 (2005) provides a statutory list of other "nontestamentary transfers" to include various types of contracts: insurance, annuity, employment, employee benefit plans, deferred compensation or pension plans, individual retirement plans, and tuition programs.

h. See generally, *In re Estate of Roloff*, 36 Kan. App.2d 684, 143 P.3d 406 (2006) (addressing issues regarding transfer-on-death deed; apply joint tenancy concepts to hold the interest vested immediately in the named donee upon the donor's death).

## C. Estates, Trusts, and Probate

### 1. Agreement among heirs that plaintiff would receive balance of funds in mother's estate is enforceable against heirs. *Rector v. Tatham*, 287 Kan. 230, 196 P.3d 364 (2008).

a. In the process of agreeing upon a conservator and guardian for their mother, Mary entered into an agreement with brother Clifford and sister Patricia. Although sister Ruth did not sign the agreement, all parties allegedly asked the judge in the consesrvator/guardian hearing to approve and incorporate the agreement into its order. Mary performed by conveying her ½ interest in her homestead to her mother.

b. The agreement provided for how they would deal with their mother's assets upon death by providing:

"The parties agree that the conservatorship and its successor arrangement will provide that in the event [mother] dies and funds remain, that the remaining balance will be payable on death to [plaintiff/Mary]."

c. Mother died and her remaining assets, approximately $50,000, were distributed evenly among the siblings pursuant to the mother's will. Mary brought suit to enforce the agreement.

d. The district court granted the defendants' motion to dismiss, holding the agreement was not a valid K.S.A. 59-102(8) settlement agreement. The Court of Appeals reversed holding Mary's claim could be supported as an assignment of an expectancy interest and

under a promissory estoppel theory.

e. Mary does not contend that the parties entered into a family settlement agreement as contemplated by K.S.A. 59-102(8). Instead she asserts the agreement is enforceable under basic contract law, independent from the probate context.

f. The Supreme Court affirms the Court of Appeals and holds:

(1) An agreement to assign an expectancy is enforceable "as long as the assignments were fair, were supported by consideration, were not induced by fraud, and were clearly indicative of the intention of the parties."

(2) Assignment of an expectancy can be made between heirs.

(3) The petition stated a claim on the assignment theory and should not have been dismissed.

(4) The petition stated a claim under a promissory estoppel theory and should not have been dismissed.

g. **BAR EXAM NOTE:** See Kansas Morning Essay Examination Question 8 (February 2008 Bar Exam), **Appendix A** to this Outline.

2. **Estate administrator can pursue assets in possession of trust beneficiaries that were transferred in breach of a prenuptial agreement.** ***Estate of Draper v. Bank of America, N.A.***, ____ Kan. ____, 205 P.3d 698 (April 17, 2009).

a. 1967 Clark and Ethel enter into an antenuptial agreement in contemplation of their marriage. The parties made mutual agreements regarding disposition of property. Ethel agreed that if she survived Clark she would maintain a valid will devising Clark's sons (by a prior marriage) "not less than one-fourth to each of them of her entire estate remaining after the payment of debts, administrative expense, taxes or other obligations."

b. 1977 Clark died testate and, in accordance with their agreement, left a substantial portion of his estate to Ethel.

c. Shortly after Clark's death Ethel set up an irrevocable trust giving Ethel the income and corpus during her life with the remainder to

various charities and individuals – but not Clark's sons.

d. 1982 Ethel executed a will which divided her estate equally among Clark's three sons. The same day she created another irrevocable trust with the same beneficiaries provided for in her 1977 trust.

e. October 2002 Ethel dies leaving a probate estate of less than $10,000. Assets in the two trusts exceeded $1,000,000.

f. January 2003, Ethel's will admitted to probate. December 2003, Clark's son, Gerald, as executor of Ethel's estate, sued the trustees and trust beneficiaries seeking to have a constructive trust imposed on the trust assets because Ethel breached her contract to give at least 3/4ths of her "entire estate" to Clark's sons.

g. The trial court ordered that the trust property be placed in a constructive trust for Clark's sons. The Court of Appeals reversed, holding Ethel complied with the explicit language of the antenuptial agreement, which did not prohibit her from gifting property or establishing trusts.

h. Constructive trust law clarified.

(1) The Supreme Court clarifies that it is not necessary to prove actual or constructive fraud in order to employ the constructive trust remedy.

(2) Relying upon the Restatement of Restitution, the Court states: "[A] constructive trust is an appropriate remedy '[w]here a person holding title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it.'"

(3) "Where, as here, a person who holds property that is subject to a beneficial interest transfers the property, an action may be brought against the third party for the return of the property."

i. Constructive fraud.

(1) Defined: "'a breach of a legal or equitable duty which, irrespective of moral guilt, the law declares fraudulent because of its tendency to deceive others or violate a confidence, and neither actual dishonesty [n]or purpose or

intent to deceive is necessary.'"

(2) "Two additional elements must also be proven in order to establish constructive fraud: (1) a confidential relationship, and (2) a betrayal of this confidence or a breach of a duty imposed by the relationship."

(3) "A 'confidential relationship' refers to any relationship of blood, business, friendship, or association in which one of the parties reposes special trust and confidence in the other who is in a position to have and exercise influence over the first party."

(4) "[A] confidential relationship can be based on an agreement between the owner of property and another who will distribute the owner's property in a specified manner upon the owner's death."

(5) "[A] confidential relationship existed between Ethel and Clark."

(6) "Kansas has repeatedly recognized a confidential relationship arises when spouses agree to leave property by will."

j. Contractual obligation and breach of duty.

(1) Court of Appeals: Ethel complied with the letter of their agreement.

(2) Supreme Court: Ethel did not comply with the spirit of the agreement.

(a) Uses implied duty of good faith and fair dealing to fill-in the spirit of the express language used.

(b) Quoting comment a to Restatement (Second) of Contracts § 205 which notes that good faith emphasizes: "'faithfulness to an agreed common purpose and consistency with the justified expectations of the other party . . . .'"

(3) "[T]he implied duty of good faith and fair dealing applied to Ethel's agreement to leave three-quarters of her estate to

Clark's sons. This duty would not allow Ethel to make gifts that are inconsistent with the justified expectations of Clark that his sons would receive three-quarters of the entire estate Ethel enjoyed at the time of her death."

(4) "Ethel removed over $1 million in assets from her estate and left $10,000 to be distributed to Clark's sons. In light of the trust Clark reposed in Ethel and the agreement they reached, her giving away virtually all of her assets to others thwarted the intent of the agreement and violated the duty of good faith that Ethel owed to Clark."

k. Nonclaim statute.

(1) K.S.A. § 59-2239(1) provides, in part:

"All demands . . . against a decedent's estate . . . shall be forever barred from payment unless the demand is presented within the later of: (a) four months from the date of first publication of notice under K.S.A. 59-2236 . . . or (b) if the identity of the creditor is known or reasonably ascertainable, 30 days after actual notice was given . . . . No creditor shall have any claims against or lien upon the property of a decedent other than liens existing at the date of the decedent's death, unless a petition is filed for the probate of the decedent's will pursuant to K.S.A. 59-2220 . . . or for the administration of the decedent's estate pursuant to K.S.A. 59-2219 . . . within six months after the death of the decedent and such creditor has exhibited the creditor's demand in the manner and within the time prescribed by this section . . . ."

(2) Clark's sons had a claim against Ethel, as third party beneficiaries to the antenuptial agreement, for breach her contractual obligations.

(a) This would have been a claim that would be subject to the nonclaim statute.

(b) Failure to make the claim within the four-month period bars the claim.

(3) However, in this case it was the executor seeking return of the assets from third parties in order to comply with the

executor's obligation to marshal assets that should be part of the probate estate.

(4) "Applying K.S.A. 59-1401, Kansas cases make clear that an action to marshal assets is properly brought by the representative of the estate and is not a claim against the estate."

(5) "[W]e conclude that the administrator could bring this action, the action was not a claim against the Estate, and the action was not barred by the failure to bring a claim against the Estate within the period of the nonclaim statute.

l. Statute of limitations.

(1) Not addressing, because not raised, the language in K.S.A. § 59-1401(c) directing the executor or administrator to "take possession, within six months from the date of appointment, of all tangible personal property . . . ." **COMMENT:** This appears to be more of a diligence standard imposed upon the executor or administrator as opposed to a statute of limitation that would bar their freedom to pursue their statutory duties.

(2) Unjust enrichment is the cause of action against the third parties who received the property from Ethel. Statute of limitations for unjust enrichment cause of action is 3 years. K.S.A. § 60-512(1) ("All actions upon . . . obligations or liabilities . . . implied but not in writing.")

(a) Issue is when did the cause of action for unjust enrichment accrue?

(b) 1977 and 1982 when the property was placed by Ethel in the trusts? No.

(c) October 2002 when Ethel died? Yes. "[I]t was only at her death when she had not fulfilled her contract that the trustees had an equitable duty to return the property or that the beneficiaries had a right to receive the property. All of the elements of unjust enrichment were present when defendants retained the property after Ethel's death."

(d) The executor brought suit on December 2003 so the lawsuit was well within the limitation period.

3. **Children must make a timely claim against their father's estate to establish basis for seeking recovery of property from third party transferees. Children's claims barred by the nonclaim statute.** ***Nelson v. Nelson***, ____ Kan. ____, 205 P.3d 715 (April 17, 2009).

a. 1975, parents divorced and entered into a property settlement agreement requiring the father to "execute and maintain, in full force and effect, a Will creating a testamentary trust to be funded by and with Husband's entire estate. Said trust will provide that the two (2) children of the parties hereto shall receive one-half (½) of the income from the trust . . . ."

b. Husband/father remarries in 1978 and remains married to his second wife until his death in 2003.

c. Husband/father makes substantial gifts to his second wife in 1987 (real property where business located), 1990 (purchased residence in wife's sole name), and designated second wife as beneficiary of pension fund.

d. When their father died he had no assets in his estate.

e. Suit was brought by the children against their father's second wife, and other recipients of gifs from his estate. The court notes: "The Appellants had not taken any action to file a petition for administration of an estate in Kansas and had not filed a claim against Albert or his estate in Florida."

f. The trial court held the claims were against their father for failing to honor the settlement agreement. Therefore, their claims were against his estate, which are now time barred. The Court of Appeals affirmed, noting it was barred by the contract provision of the nonclaims statute. Supreme Court: "This claim against Albert's estate is barred by the Appellant's failure to exercise the right of creditors to open an estate and make a timely claim as required by K.S.A. 59-2239(1)."

g. More constructive trust jurisprudence:

(1) A remedy, not a cause of action.

(2) The claim, or cause of action need not be limited to constructive fraud or fraud. Other claims, such as unjust enrichment, can support the constructive trust remedy.

(3) "[W]e conclude the view that actual or constructive fraud must be established before the remedy of a constructive trust can be granted is contrary to widely accepted analysis of the remedy and is not justified by Kansas law. To the extent that any case has held that actual or constructive fraud is the exclusive basis for the remedy of constructive trust, we explicitly disapprove that holding."

h. More nonclaim statute jurisprudence:

(1) "[A] person who seeks to recover from the decedent, whether based on tort, contract, the decedent's will, or the statute of intestate succession, must recover, if at all, from the decedent's estate."

(2) "K.S.A. 59-2239 imposes a special statute of limitations governing such claims against a decedent's estate, and it operates as a complete bar to all demands against a decedent's estate that are not timely filed."

(3) "Kansas appellate cases are in accord and have consistently held that an action to enforce an agreement to devise or bequeath a portion of the decedent's estate constitutes a claim against the estate."

(4) "When one claims property of an estate, the fact that an estate does not exist does 'not relieve [a family member] or any other person having a claim upon the property of [the] estate from having an administrator appointed' under the provisions of K.S.A. 59-2239 and making a claim against the estate."

(5) "[W]e hold that the Appellants as third-party beneficiaries asserted a claim against the estate by alleging that Albert's transfers of assets to the trust were a breach of the property settlement agreement and, therefore, the transfers were void. This claim against Albert's estate is barred by the Appellant's failure to exercise the right of creditors to open an estate and make a timely claim as required by K.S.A. 59-2239(1)."

4. **Beneficary of will can claim "innocent beneficiary" status under K.S.A. § 59-618 when beneficary's own attorney failed to present will for probate within 6-month limitations period.** ***In re Estate of Seth,*** 40 Kan. App.2d 824, 196 P.3d 402 (2008).

a. K.S.A. § 59-617 provides:

"No will of a testator who died while a resident of this state shall be effectual to pass property unless a petition is filed for the probate of such will ***within six months after the death of the testator***, except as hereinafter provided." (Emphasis added).

b. K.S.A. § 59-618 provides:

"Any person who has possession of the will of a testator dying a resident of this state, or has knowledge of such will and access to it for the purpose of probate, and knowingly withholds it from the district court having jurisdiction to probate it for more than six months after the death of the testator shall be liable for reasonable attorney fees, costs and all damages sustained by beneficiaries under the will who do not have possession of the will and are without knowledge of it and access to it. ***Such will may be admitted to probate as to any innocent beneficiary on petition for probate by any such beneficiary, if such petition is filed within 90 days after such beneficiary has knowledge of such will and access to it,*** except that the title of any purchaser in good faith, without knowledge of such will, to any property derived from the fiduciary, heirs, devisees or legatees of the decedent, shall not be defeated by the production of the will of such decedent and the petition for probate of the will after the expiration of six months from the death of the decedent.

The provisions of this section as amended by this act shall apply retroactively to the withholding of a will of a testator." (Emphasis added).

c. Laryl Seth is the beneficiary of a will in which his mother, Marvel, left the 320-acre farm to Laryl. Marvel died on December 4, 2005. In February 2006 Laryl, and his sister Loyola, found the will and hired Kenneth McClintock, an attorney, to have the will admitted to probate. Laryl was assured by his attorney, McClintock, in April and May 2006 that he was "taking care of" the will.

d. The 6-month period in which the will must be presented for probate,

pursuant to K.S.A. § 59-617, expired in early June of 2006. The deadline was missed and McClintock admitted he failed to deal with it properly.

e The Court of Appeals notes: "McClintock possessed no assets or insurance to respond to a judgment, and he ultimately relinquished his law license in connection with disciplinary proceedings that resulted from his inaction on Laryl's behalf." COMMENT: Why does McClintock's ability to respond in damages for breach of the attorney/client contract matter?

f. Laryl ultimately got the will back from McClintock and hired another attorney to file it for probate, which was done in late August 2006.

g. Laryl's attempt to offer the will for probate beyond the 6-month period was contested by the three children of Laryl's brother, Lowell, who predeceased his mother Marvel. Under the law of intestacy, which applies unless the will can be probated, the farm would pass as follows applying K.S.A. § 55-506:

| | |
|---|---|
| Son Laryl | Undivided 1/3rd |
| Daughter Loyola | Undivided 1/3rd |
| Son Lowell (deceased) | Undivided 1/9th to each of Lowell's three surviving children. |

h. Laryl, however, argues he is an "innocent beneficiary" under K.S.A. § 59-618 and therefore has 90 days from the time he retrieved the will from McClintock to file it for probate.

(1) If the will is admitted to probate, Laryl will take all the farm to the exclusion of Loyola and Lowell's children.

(2) The trial court agreed with Laryl; the Court of Appeals affirms.

i. The Court of Appeals reasons:

(1) "'Innocent beneficiary' under the statute means a beneficiary without fault for the knowing withholding of a will from probate during the 6-month period following the death of the testator."

(2) The Court holds that Marvel's will was "knowingly withheld

from probate" by McClintock.

(3) The Court holds that Laryl "was 'innocent' inasmuch as he did not knowingly withhold the will from probate; in fact, he sought to probate the will and engaged counsel to effect the filing."

(4) The Court in effect holds that it is possible for a beneficiary to have both knowledge and access to a will, but they can subsequently become without access once they give it to their negligent attorney. The Court notes: "The knowledge and access referred to in the savings clause can only occur *after* the withholding and with reference to a will knowingly withheld."

(5) Just in case, the Court notes: "Our conclusion is also consistent with public policy in Kansas that favors probating every legally executed will and does not favor suppressing a will or withholding it from probate by narrow and technical applications of the statutes governing probate."

i. **COMMENT:** Nowhere in the opinion is the term "agency" mentioned.

(1) It would appear that possession by McClintock is the same as possession by his client, Laryl. McClintock is Laryl's agent for the specific purpose of offering the will to probate.

(2) K.S.A. § 59-618 was obviously adopted to protect against situations where a third party takes possession of the will, or otherwise conceals its existence, in order to negate its effect. It was not designed to protect the very beneficiary who knows of the will, has possession of the will, but simply makes a bad choice of agents to probate the will.

(3) The Court's tortured analysis is designed to do one thing: provide Laryl with recovery because his negligent, uninsured attorney was judgment proof.

(4) This injects a form of equity into this basic statute of limitations that could not have been anticipated by the legislature. It opens the door for all kinds of exceptions meaning title to property will not be settled in a timely

manner.

(5) The real public policy in this area: prompt, final adjudication of rights to property owned by the decedent. This decision runs counter to that policy.

5. **Revocable trust created by husband and wife was "joint, mutual, and contractual" and could not be amended to change rights of beneficiaries by wife after husband's death.** ***Mangels v. Cornell***, 40 Kan. App.2d 110, 189 P.3d 573 (2008).

a. 1996: Bud and Thelma, husband and wife, created a revocable trust and transferred farm land and mineral rights to the trust.

(1) Net income would be paid to Bud and Thelma, or the survivor, during their lives.

(2) Thereafter income would be paid to their three children, Darrel, Carl, and Judith.

(3) When the children died, their share would be paid to their children, per stirpes.

b. 2004: Bud dies in March and in September Thelma amends the trust to change the successor trustee provisions. In December Thelma amends the trust to pay the first $1,000,000 of trust income, at her death, to Judith, instead of dividing all trust income equally between the three children.

(1) Darrel and Carl challenged the amendments made solely by Thelma following Bud's death.

(2) Trial court holds the trust allowed Thelma to make the amendments.

(3) Court of Appeals holds the trust was joint, mutual, and contractual, and the trust expressly required both of the trust settlors to agree on amendments and therefore it could not be amended by Thelma without the consent of Bud.

c. The trust contained the following "revocability" clause:

"'13. REVOCABILITY. This trust shall be revocable, and the

*Grantors* expressly acknowledges *they* shall have the right or power, whether *alone* or in conjunction with others, and in whatever capacity, to alter, amend, revoke, or terminate this trust, or any of the terms of this Agreement, in whole or in part.'" (Emphasis by the Court).

d. The Court focuses on the plural terms "Grantors" and "they" and notes that the term "alone" refers to what "they" can do. The Court concludes that the "in conjunction with others" refers to a guardian or conservator that might be appointed to represent one of the settlors, who could join with the other spouse to create the "they" to ament the trust.

e. Other language within the four corners of the trust document:

(1) Consideration clause states: "in consideration of the foregoing and *mutual covenants and agreements* herein contained." (Emphasis by the Court).

(2) The Court of Appeals has construed similar language as creating a joint, mutual, and contractual relationship between the parties to the document.

(3) The trust guards against unilateral decisions by in several places requiring joint action.

f. Apply the seven factors to consider when determining whether the instrument is contractual:

(1) Provision for distribution of property at the death of the survivor. Present.

(2) Provision for disposition of property in the event of a lapsed residuary bequest. Not present.

(3) Use of plural nouns. Present (10 plural, 2 singular).

(4) Joinder and consent language. Present.

(5) Identical distribution of property on the death of the survivior. Present.

(6) Joint revocation of former wills. Not present (but would not

expect it with an inter vivos trust).

(7) Consideration such as "mutual promises." Present.

g. Court concludes: "Our application of the seven factors supports our conclusion that the trust is contractual in nature, with five factors supporting contractual intent, one factor to the contrary, and one factor of no application."

h. Although the Court concludes the trust instrument is not ambiguous, even if it were, the extrinsic evidence proffered in the case supports the conclusion that the trust could not be unilaterally amended by Thelma under these facts.

6. **Stepmom/Administrator properly determined ownership of property that was part of her deceased husband's estate; homestead and spousal allowances proper.** ***In re Estate of Lane***, 39 Kan. App.2d 1062, 188 P.3d 23 (2008).

a. This was the second marriage for both Jerry and Deanna. Deanna owned a 247-acre farm at the time she married Jerry. They operated a cattle business on the farm together and both held jobs in addition to the cattle business. They also acquired farm equipment, paid for, primarily, out of joint bank accounts.

b. Jerry died in 2004 and Deanna was appointed administrator of his estate. Deanna's inventory of Jerry's estate included one-half the value of the cattle and farm equipment; she did not include the farm, or any of the gas storage lease or cell phone tower lease associated with the farm.

c. Jerry's children, and grandchildren, brought suit asserting all of the value associated with the cattle and farm equipment belonged to Jerry, that the farm should has been included as an asset of the estate, and the trial court erred by awarding Deanna a $35,000 spousal allowance plus a $35,000 homestead allowance.

d. As Judge Leben observed: "In sum, the other heirs seek to increase their inheritance by removing the allowances taken from Jerry's estate and by including the farm, the leases, and the full value of the farm equipment and cattle in the estate."

e. The farm, and assets associated with the farm (gas storage and cell

phone tower leases).

(1) Deanna owned the farm when she married Jerry. There was no issue about how Deanna acquired her interest in the farm.

(2) There was no agreement about how the farm would be divided upon the death of one of them. The district court concluded: "their intent was that the survivor could do whatever they wanted to with the farm."

(3) The farm was properly excluded from Jerry's estate.

(4) Jerry and Deanna joined in a gas storage lease and cell phone tower lease covering the farm.

(a) Court notes Jerry's joinder was to ensure it would survive a claim Jerry may have in the real estate in the event of divorce. "For example, if either Jerry of Deanna had filed for divorce, Kansas law would then have given each an ownership interest in the other's separate property pending the resolution of the divorce. See K.S.A. 23-201(b)."

(b) Another consideration would be K.S.A. § 59-505 which provides in part:

"[T]he surviving spouse shall be entitled to receive one-half of all real estate of which the decedent may at any time during the marriage was seized or possessed and to the disposition whereof the survivor shall not have consented in writing, or by a will, or by an election as provided by law to take under a will . . . ."

(c) Although the property was titled only in Deanna's name, to protect the gas storage lessee, and the cell phone tower lessee, in the event Deanna predeceased Jerry, they would presently obtain Jerry's signature on the leases so "the disposition whereof the survivor" will have "consented in writing" as contemplated by K.S.A. § 59-505.

(5) Court observes: "Thus, like the future payments for future oil

and gas exploration, a lease for future use of the real estate constitutes an interest in that real estate, not personal property."

(a) The continuing lease payments are treated as real property and follow the ownership of the farm.

(b) "It would be an odd legal rule indeed that would give Jerry's estate the right to receive payments for the continued use of Deanna's real estate after his own death."

f. The cattle and farm equipment. Although only Jerry's name was listed on some of the titles and bills of sale for the personal property, this does not prevent Deanna from being a co-owner.

(1) "[M]arried couples are not required to document their status as co-owners of their personal property. The parties intent and conduct determine whether personal property is co-owned when acquired during a marriage."

(2) The evidence supported a finding that the intent and conduct of the parties was to have equal ownership in the property they acquired to run their cattle business. Purchases using joint bank accounts; both actively involved in the cattle business. They viewed themselves as co-owners of the business and its assets.

g. The spousal allowance. K.S.A. § 59-403 provides, in part:

"When a resident of the state dies, testate or intestate, the surviving spouse shall be allowed, for the benefit of such spouse and the decedent's minor children during the period of their minority, from the personal or real property of which the decedent was possessed or to which the decedent was entitled at the time of death, the following:

. . . .

(b) A reasonable allowance of not more than $35,000 in money or other personal property or real property at its appraised value in full or part payment thereof, with the exact amount of such allowance to be determined and ordered by the court, after taking into account the condition of the estate of the decedent.

The property shall not be liable for the payment of any of

decedent's debts or other demands against the decedent's estate, except liens thereon existing at the time of the decedent's death. If there are no minor children, the property shall belong to the spouse . . . ."

(1) The plaintiffs asserted the surviving spouse should not have been awarded a $35,000 spousal allowance because the trial court failed to consider whether she needed the allowance.

(2) "Under the statute, the district court 'has complete discretion to determine the amount of any such allowance.'"

(3) "The other heirs have not demonstrated that it was an abuse of discretion to award this allowance to Deanna, a retired teacher, even though it depleted the overall assets in the estate."

h. The homestead allowance. K.S.A. § 59-6a215 provides:

"A surviving spouse is entitled to the homestead, or in lieu thereof the surviving spouse may elect to receive a homestead allowance of $35,0000. The homestead or homestead allowance is in addition to any share passing to the surviving spouse by way of elective share."

(1) "The other heirs challenge the award of the homestead allowance based on the finding that Deanna already owns a home."

(2) "As Deanna has not received 'the homestead' from the estate, nothing in the statutory language prohibits her from taking a homestead allowance 'in lieu thereof.'"

(3) "The homestead allowance, unlike the statutory spousal allowance, in an entitlement. The legislature has said that the surviving spouse 'is entitled' to it. The homestead allowance is an important right that should not be limited by any condition unless the statute clearly provides that limitation."

(4) Deanna was entitled to the homestead allowance.

## D. On The Farm

### 1. Farmer's water right lost for non-use without "due and sufficient cause." *Frick Farm Properties v. Kansas Department of Agriculture*, 40 Kan. App.2d 132, 190 P.3d 983 (2008).

a. November 4, 1982 a certificate of appropriation was issued to Debes for a water right on farm land. Frick purchased the land from Debes in 2002, including the water right. January 2003 Debes was notified by the Kansas Division of Water Resources (DWR) that water had not been used under the right for 3 years and it would be terminated if the period of nonuse extended to 5 years. A similar notice was received in 2004 requesting Frick to report the reasons for the nonuse. Frick replied stating that Debes' ongoing health problems prevented him from using the water right and Frick had just purchased the property in October 2002.

b. Report by the DWR indicated that for years 1985 through 2003 there was nonuse of the water right without due and sufficient cause. Following a hearing the chief engineer issued an order terminating the water right. The Secretary of Agriculture denied Frick's petition for review. The district court affirmed the DWR order.

c. On appeal, Frick argues the water right was a real property right and that DWR committed numerous errors in terminating the water right. The Court of Appeals affirms the DWR's termination of Frick's water right.

d. Water in Kansas is a "statutory" real property right.

(1) K.S.A. § 82a-701(g) defines "water right" as:

> "[A]ny vested right or appropriation right under which a person may lawfully divert and use water. It is a real property right appurtenant to and severable from the land on or in connection with which the water is used and such water right passes as an appurtenance with a conveyance of the land by deed, lease, mortgage, will, or other voluntary disposal, or by inheritance."

(2) The state may create the property right by statute and in the process place conditions on the property right.

(3) K.S.A. § 82a-718(a) places conditions on the water right:

"Every water right of every kind shall be deemed abandoned and shall terminate when without due and sufficient cause no lawful, beneficial use is henceforth made of water under such right for five successive years. Before any water right shall be declared abandoned and terminated the chief engineer shall conduct a hearing thereon. . . ."

(4) Under K.S.A. § 82a-718(b)(3) "the right will not be terminated if the user shows that for one or more of the five consecutive years the beneficial use of the water was prevented or made unnecessary by circumstances that are due and sufficient cause for nonuse . . . ."

e. The court concludes the DWR followed the proper termination procedures and since Frick failed to present any "due and sufficient cause for nonuse," his water right was properly terminated.

2. **Farmer required to obtain a permit to obstruct stream that no longer exists, but once existed sometime after 1929.** ***Frank v. Kansas Department of Agriculture, Division of Water Resources***, 40 Kan. App.2d 1024, 198 P.3d 195 (2008).

a. Frank obtained a permit, from the chief engineer of the Kansas Division of Water Resources, to appropriate water for recreational purposes by collecting it in a "groundwater pit" on his land.

(1) Kan. Admin. Reg. § 5-22-1(x) defines "groundwater pit" as "an excavation in the earth" that meets the following criteria: "(1) Exposes the current or historic groundwater table; (2) has caused, or will likely cause, annual evaporation of groundwater; and (3) has a perimeter equal to or greater than the depth of the excavation."

(2) As a condition of the permit, Frank was required to construct an embankment around the groundwater pit to prevent surface water from entering the pit.

(3) Frank constructed the pit and the embankment as required by his permit.

(4) The permit also contained language that it granted Frank no

authority to obstruct a "stream."

(5) After completing the groundwater pit and embankment Frank's neighbor complained about water backing up on the neighbor's property.

(6) The chief engineer informed Frank he had to apply for another permit because he had obstructed a stream which caused the change in water flow.

(7) The chief engineer and the district court all concluded that Frank had improperly obstructed a stream and was required to apply for permission before making any obstruction.

b. K.S.A. § 82a-301(a) prohibits, without prior authorization from the chief engineer, the construction of any structure on land that could "change or diminish the course, current, or cross section of any stream within the state."

(1) The statute does not define the word "stream."

(2) K.S.A. § 82a-301 and related statutes grant the chief engineer authority to adopt regulations "to establish standards for the construction, modification, operation and maintenance" of stream obstructions and "to administer and enforce" the stream obstruction statutes.

(3) Kan. Admin. Reg. § 5-40-1(k) is the chief engineers exercise of the statutory authority by defining "stream" to mean: ***"any watercourse that has a well-defined bed and banks"*** so long as it "has a watershed above the geographic point in question that exceeds" certain acreage requirements.

(a) There is no dispute that the watershed acreage requirements have been met.

(b) The issue concerns the next part of the regulation that creates a presumption that a stream exists, or existed at sometime after 1929, which must be rebutted by the landowner to avoid the permit requirement.

(4) The major issue is a presumption the regulation creates by providing:

"The stream need not flow continuously and may flow only briefly after a rain in the watershed. If the site of the project has been altered so that determination of whether the well-defined bed and banks exist is not possible, it shall be presumed that they did exist if the watershed acreage criteria have been met, unless the owner of the project can conclusively demonstrate that the well-defined beds and banks did not exist before the construction of the project."

(a) Because the stream obstruction law did not take effect until 1929, the Division does not require proof of the absence of a stream before 1929.

(b) The net effect of the regulation is anyone proposing to build in a watershed meeting the acreage criteria, must first ascertain if the location will impact a stream that currently exists on the property, or may have existed at any time since 1929 – even though its bed and banks are no longer identifiable by being "well-defined."

c. The issue is whether the chief engineer has the statutory authority to impose the presumption.

(1) The Court of Appeals does not address this precise question because it finds, in this case, the presumption was justified because the stream in fact existed at this location and in fact caused problems when it was obstructed.

(2) The Court avoids answering the question by, in effect, accepting the evidence offered by the Division which proves the existence of a stream at the location.

(3) The Court finds the chief engineer, under these facts, acted rationally in requiring a permit.

d. **NOTE:** Although the Court does not purport, at one part of its opinion, to address the underlying validity of the regulation, its concluding statement seems to indicate the presumption was valid, and was properly applied. The Court concludes by stating:

"In sum, the chief engineer's valid regulation contains a presumption that a stream previously existed within a watershed area

of sufficient size. That regulation was applicable to Frank's property, which was part of a substantial watershed area. Under the regulation, Frank had the burden to show that there had not previously been a stream located where he placed his obstruction. Frank failed to do so. The agency's application of this presumption was not unreasonable in Frank's case based upon the evidence that a stream had once existed there."

e. **COMMENT:** So this case stands for the proposition that the presumption created by the regulation is valid whenever the Division can prove a stream in fact existed at the location? This seems like a lot of litigation over the validity of a regulation without any definitive resolution of the underlying issue. It tells us the answer in Frank's case but tells us very little about the validity of the regulation that was the focus of Frank's case.

## KANSAS MORNING ESSAY EXAMINATION QUESTION 8

Jake was a farmer and upon his death wanted to pass his farmland to his only child, Frank. Jake met with his attorney who suggested a Kansas Transfer on Death Deed be used to transfer title to Frank. Jake agreed and the properly prepared and executed Transfer on Death Deed was recorded in the office of the Register of Deeds. Jake was not married at the time he executed the Deed and remained single until his death.

After the deed was properly recorded, Jake gave the Transfer on Death Deed to Frank for safekeeping.

A year later, Frank experienced financial difficulties and showed his friend, Joe, the recorded Transfer on Death Deed. He offered to sell Joe his interest in the farm for $20,000 with the conveyance to be made by Quitclaim Deed. Joe agreed and paid Frank $20,000. Frank and his wife Angela executed a properly prepared Quitclaim Deed to Joe describing the farmland which deed was recorded in the office of the Register of Deeds.

Frank's financial difficulties continued, and a year later he approached Mark with the same proposal. Mark agreed except that he required the conveyance to him be made by a Warranty Deed rather than a Quitclaim Deed. Frank agreed. Mark paid Frank $20,000 and Frank delivered his executed Warranty Deed to Mark describing the farmland which deed states in part that Frank "conveys and warrants to Mark an indefeasible estate in fee simple absolute." Frank's wife Angela did not sign the Warranty Deed. The Deed was recorded in the office of the Register of Deeds.

Jake died a year later. A dispute arose among Joe, Mark, Frank, and Angela as to ownership of the farmland. The matter was tried to the judge.

For purposes of answering the following questions, do not discuss equitable or potential tort claims. Please confine your answers to analysis of the rights and obligations under the instruments used and statutory law.

**Part 1: What arguments will Joe make in support of his position that he owns either part or all of the farmland?**

**Question 8 continues on the next page**

**Part 2:** **What arguments will Mark make in support of his position that he owns either part or all of the farmland?**

**Part 3:** **What arguments will Frank and Angela make in support of their position that either or both own either part or all of the farmland?**

**Part 4:** **Whom should the judge determine to be the owner(s) of the farmland and why? If you have not already done so in your answers to prior parts of this question, include within your analysis a description of the purpose of each instrument (i.e., Transfer on Death Deed, Quitclaim Deed, and Warranty Deed) and how each differs from the others.**

## APPENDIX B

**16-121. Construction contracts, motor carrier transportation contracts, dealer agreements, franchise agreements; certain indemnification provisions and additional insured provisions void, when.**

**(a)** When used in this section:

**(1)** "Construction contract" means an agreement for the design, construction, alteration, renovation, repair or maintenance of a building, structure, highway, road, bridge, water line, sewer line, oil line, gas line, appurtenance or other improvement to real property, including any moving, demolition or excavation, except that no deed, lease, easement, license or other instrument granting an interest in or the right to possess property shall be deemed to be a construction contract even if the instrument includes the right to design, construct, alter, renovate, repair or maintain improvements on such real property. "Construction contract" shall not include any design, construction, alteration, renovation, repair or maintenance of: (A) Dirt or gravel roads used to access oil and gas wells and associated facilities; or (B) oil flow lines or gas gathering lines used in association with the transportation of production from oil and gas wells from the wellhead to oil storage facilities or gas transmission lines.

**(2)** "Contract" means any construction contract, motor carrier transportation contract, dealer agreement or franchise agreement.

**(3)** "Damages" means personal injury damages, property damages or economic loss.

**(4)** "Dealership agreement" means an oral or written agreement of definite or indefinite duration between an equipment manufacturer or service provider and an equipment or service dealer which provides for the rights and obligations of the parties with respect to the purchase or sale of such equipment or services.

**(5)** "Franchise agreement" means any contract or franchise or any other terminology used to describe the contractual relationship between manufacturers, distributors and dealers, by which:

**(A)** A right is granted one party to engage in the business of offering, selling or otherwise distributing goods or services under a marketing plan or system prescribed in substantial part by the other party, and in which there is a community of interest in the marketing of goods or services at wholesale or

retail, by lease, agreement or otherwise; and

**(B)** the operation of the grantee's business pursuant to such agreement is substantially associated with the grantor's trademark, service mark, trade name, logotype, advertising or other commercial symbol designating the grantor or an affiliate of the grantor.

**(6)** "Indemnification provision" means a covenant, promise, agreement, clause or understanding in connection with, contained in, or collateral to a contract that requires the promisor to hold harmless, indemnify or defend the promisee or others against liability for loss or damages.

**(7)** "Motor carrier transportation contract" means, with respect to a motor carrier as defined in K.S.A. 66-1,108, and amendments thereto, a contract, agreement or understanding covering:

**(A)** The transportation of property by a motor carrier;

**(B)** the entrance on property by the motor carrier for the purpose of loading, unloading or transporting property; or

**(C)** a service incidental to activity described in clause (A) or (B) including, but not limited to, storage of property.

"Motor carrier transportation contract" shall not include the uniform intermodal interchange and facilities access agreement administered by the intermodal association of North America or other agreements providing for the interchange, use or possession of intermodal chassis, containers or other intermodal equipment.

**(8)** "Mutual indemnity obligation" means an indemnity obligation in a contract in which the parties agree to indemnify each other and each other's contractors and their employees against loss, liability or damages arising in connection with bodily injury, death and damage to property of the respective employees, contractors or their employees, and invitees of each party arising out of or resulting from the performance of the agreement.

**(9)** "Promisee" shall include an agent, employee or independent contractor who is directly responsible to the promisee.

**(10)** "Unilateral indemnity obligation" means an indemnity obligation in a contract in which one of the parties as promisor agrees to indemnify the other party as promisee with respect to claims for personal injury or death to the promisor's employees or agents or to the employees or agents of the promisor's contractors but in which the promisee does not make a reciprocal indemnity to

the promisor.

**(b)** An indemnification provision in a contract which requires the promisor to indemnify the promissee for the promissee's negligence or intentional acts or omissions is against public policy and is void and unenforceable.

**(c)** A provision in a contract which requires a party to provide liability coverage to another party, as an additional insured, for such other party's own negligence or intentional acts or omissions is against public policy and is void and unenforceable.

**(d)** This act shall not be construed to affect or impair:

**(1)** The contractual obligation of a contractor or owner to provide railroad protective insurance or general liability insurance;

**(2)** an agreement under which an owner, a responsible party or a governmental entity agrees to indemnify a contractor directly or through another contractor with respect to strict liability under environmental laws;

**(3)** an indemnification agreement that is an integral part of an offer to compromise or a settlement of a disputed claim, if: **(A)** The settlement is based on consideration; **(B)** the dispute relates to an alleged event that is related to a construction contract and that occurred before the settlement is made; and **(C)** the indemnification relates only to claims that have arisen or may arise from the past event;

**(4)** the validity of any insurance contract, construction bond or other agreement lawfully issued by an insurer or bonding company;

**(5)** a separately negotiated provision or provisions whereby the parties mutually agree to a reasonable allocation of risk, if each such provision is: (A) Based on generally accepted industry loss experience; and (B) supported by adequate consideration; and

**(6)** an agreement that provides for indemnity if the parties agree in writing that the indemnity obligation will be supported by liability insurance coverage to be furnished by the promisor subject to the following limitations:

**(A)** With respect to a mutual indemnity obligation, the indemnity obligation is limited to the extent of the coverage and dollar limits of insurance or qualified self-insurance each party as promisor has agreed to obtain for the benefit of the other party as promisee.

**(B)** With respect to a unilateral indemnity obligation, the indemnity obligation is limited to the extent of the coverage and dollar limits of insurance the

promisor has agreed to obtain for the benefit of the other party as promisee. Such indemnity obligation shall be at the promisee's expense and shall be a separate liability insurance policy.

**(e)** Notwithstanding any contractual provision to the contrary, the laws of the state of Kansas shall apply to and govern every contract to be performed in this state. Any litigation, arbitration or other dispute resolution proceeding arising from such contract shall be conducted in this state. Any provision, covenant or clause in such contract that conflicts with the provisions of this subsection shall be void and unenforceable.

**(f)** This section applies only to indemnification provisions and additional insured provisions entered into after January 1, 2009.

**History:** L. 2004, ch. 70, § 1; L. 2008, ch. 132, § 1; Jan. 1, 2009.

# Recent Developments in Kansas Business, Contract, and Property Law

by

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1

## Becker v. Knoll

- Becker is a shareholder in the Finney County Water Users Association.
- Knoll is the president of the Association.
- Becker sued Knoll asserting Knoll breached his fiduciary duty owed the Association by using an Association employee for his personal work.
- **Issue: shifting burdens of proof.**

2

## Becker v. Knoll

- Becker has initial obligation to make out a prima facie case of self-dealing.
- If Becker establishes a prima facie case, the Burden then shifts to Knoll to establish that his actions were in good faith.
- Arguably Becker failed to make out a prima facie case.
- In any event, Knoll rebutted any presumption of unfaimess.

3

## Kansas Heart Hospital v.Idbeis

- KHH controlled by Cardiac Health of Wichita, Inc. (CHW) and Cardiac Associates of Wichita, Inc. (CAW).
- 2000: CHW bylaws amended to limit shareholder ownership in facilities that compete with KHH.
- Bylaw established a buyout formula based on purchase price and Consumer Price Index adjustment.

4

## Kansas Heart Hospital v.Idbeis

- 2004: Several CHW shareholders invested in a competing facility.
- 2005: CHW Board redeemed the doctor's shares relying upon the bylaw.
- **Issue: can this be done through a bylaw as opposed to an amendment to the articles of incorporation?**

5

## Kansas Heart Hospital v.Idbeis

- Yes. This limitation on individual stock ownership can be imposed through bylaw.
- If the restriction relates to an entire "class" of stock, it must be done through the articles of incorporation.
- If the restriction is an "ownership restriction" it can be imposed either in the articles of incorporation, the bylaws, or by agreement.

6

## Kansas Heart Hospital v.Idbeis

- Use of the term "redemption" in the bylaw means "purchase" when considered in context.
- **Issue: Will the Board's determination the doctors were investing in a "competing health care facility" be tested by the "business judgment rule"?**

7

## Kansas Heart Hospital v.Idbeis

- Applying the bylaw to the facts at hand was a business judgment of the board subject to the business judgment rule.
- The directors were disinterested and informed and acted in good faith.
- Their actions satisfied the business judgment rule – even if their decision may have been the wrong decision.

8

## Foundation Property Investments v. CTP

- CTP borrowed money to purchase a truck stop.
- The note provided that if payments were not made when due: **"the whole amount shall become immediately due and payable at the option of the holder without notice."**
- Nine consecutive payments were made and accepted late without complaint.

9

## Foundation Property Investments v. CTP

- Following the ninth late payment Foundation informed CTP it was accelerating the note and demanded payment in full.
- CTP argued Foundation had waived its right to timely payment.
- Foundation argued it had not elected to exercise its "option" to accelerate, until now.

10

## Foundation Property Investments v. CTP

- **Issue: had Foundation waived its right to demand acceleration by accepting the nine late payments?**
- The Court holds Foundation had waived its right to exercise its option to accelerate; at least until it gave CTP notice that future payments must be made in a timely manner.

11

## Foundation Property Investments v. CTP

- Court notes the document did not contain an anti-waiver clause.
- Dissenting Justice Brier believed the optional nature of the acceleration clause avoided the waiver issue and the need for an anti-waiver clause.
- **COMMENT:** A "good faith" analysis could harmonize the positions of the Court and Justice Brier.

12

## Foundation Property Investments v. CTP

- **COMMENT:** Although Foundation had the right – the option – to decide whether to accelerate, by its actions it may have led CTP to reasonably believe timely payment was not required.
- This could trigger a good faith obligation in the "enforcement" of the contract to notify CTP that future payments must be timely or Foundation may elect to accelerate.

13

## Foundation Property Investments v. CTP

- **COMMENT:** It is possible to negate any sort of good faith obligation by spelling out, in the note, that Foundation can, after a period of accepting late payments, immediately insist, without notice, upon its right to accelerate for a lack of timely performance.
- This also negates any opportunity to imply a good faith obligation to notify.

14

## American General Financial Services v. Carter

- 2001: Jeff fails to pay sales taxes resulting in the KDR filing a tax lien.
- 2004: Jeff buys a home financed through American General.
- 2005: KDR files two additional tax liens.
- 2006: Jeff defaults on his home loan and American General forecloses.
- **Issue: What are the relative rights of KDR and American General in the foreclosure sales proceeds?**

15

## American General Financial Services v. Carter

- District Court: KDR has priority for its 2001 tax warrant over American General's 2004 mortgage.
- Court of Appeals: American General's purchase money mortgage has priority over all of KDR's liens.
- Tax warrant has the status of a "judgment" which is junior to a purchase money mortgage.

16

## American General Financial Services v. Carter

- We are not dealing with a lien on property being sold by a seller.
- Instead, we are dealing with a lien against a buyer of property who has no interest in the property until it is acquired using the mortgagee's money.

17

## Independent Financial v. Wanna

- Intricacies of the Kansas Uniform Consumer Credit Code.
- "Supervised loan" is a consumer loan where the annual percentage rate exceeds 12%.
- To assert rights as an assignee of a "supervised loan" you must qualify as a "supervised lender."

18

## Independent Financial v. Wanna

- Although the original lender, Ditech, was a "supervised lender" its assignee, Independent Financial, was not.
- At the foreclosure proceeding Independent Financial asserted rights under a workout agreement with the debtors. Other creditors were able to prevent Independent Financial from participating in the foreclosure because it did not qualify as a "supervised lender."

19

## Deutsche Bank National Trust Co. v. Rooney

- 2004, May: Thomas quits making court-ordered support payments to Kathleen.
- 2004, October: Nu-Dell obtains a judgment against Thomas.
- 2004, December: Thomas enters into a mortgage on his residence with Bank.
- 2005: Bank seeks to foreclose on mortgage because Thomas is not paying.

20

## Deutsche Bank National Trust Co. v. Rooney

- Kathleen and Nu-Dell's judgment liens will not attach to Thomas' homestead.
- Bank's mortgage was a consensual lien which did attach to Thomas' homestead.
- **Issue: Once the Bank begins foreclosure on the homestead, can Kathleen and Nu-Dell's liens attach to the homestead? If so, will Kathleen and Nu-Dell have priority for their claims?**

21

## Deutsche Bank National Trust Co. v. Rooney

- The non-consensual liens cannot attach to the homestead.
- Relying upon *Morris v. Ward* (1869), "only those liens specifically excepted from the homestead exemption can attach to homestead property."
- Kathleen and Nu-Dell cannot satisfy their debts out of funds generated by a foreclosure sale of Thomas' homestead.

22

## Hodges v. Johnson

- Johnson sold Hodges a 10-year-old car with 135,945 miles on it for $15,900.
- The air conditioner quit working shortly after Hodges bought it; Johnson refused to pay to repair the air conditioner.
- Hodges sues in small claims court and obtains a judgment for $3,474.
- Johnson appeals; district court affirms.

23

## Hodges v. Johnson

- Court of Appeals: 2/1 reverses trial court holding the implied warranty of merchantability on a used car does not include the air conditioning system.
- Supreme Court: Yes it does; and the trial court erred by failing to award attorney fees to Hodges; and the Supreme Court awards $4,106.50 for the appeal to the Supreme Court.

24

## Hodges v. Johnson

- Application of the implied warranty of merchantability to used goods.
- Was the failure of the air conditioner within the scope of the seller's warranty? Yes.
- Hodges must prove: car was defective, at the time of the sale, and the defect caused injury.
- Hodges met his burden.

25

## Hodges v. Johnson

- **COMMENT:** What there an express warranty?
- Johnson: "just pretty much a perfect car."
- Court used it to define the scope of the implied warranty.
- Johnson also indicated he had been driving the car as his personal vehicle for the past 2 years.

26

## Hodges v. Johnson

- **COMMENT:** The Court's holding is a boost to small claims court.
- K.S.A. § 61-2709 imposes a mandatory duty to award attorney fees when the appellee is successful on appeal.
- Benefits the consumer/claimant who is typically not likely to appeal an adverse ruling.

27

## Hurst Enterprises v. Crawford

- Cactus Roofing issued a check to Hernandez.
- Hernandez cashed the check with Hurst.
- Cactus stopped payment on the check three days after Hurst gave value for it.
- Hurst sues to recover on the check.
- Hurst is a holder in due course under K.S.A. § 84-3-302.

28

## Hurst Enterprises v. Crawford

- **Issue: Is Hurst subject to a § (d) set-off under 84-3-302 because Hernandez had only partially performed the roofing work for which he was paid by Cactus Roofing?**
- Held: No. § (d) does not focus on the performance of the payee (Hernandez) but rather performance by the holder (Hurst). Here Hurst fully performed by paying value for the check so § (d) does not apply.

29

## Carrothers Construction Co. v. City of South Hutchinson

- During last year's recent developments I noted the apparent conflict in the liquidated damages analyses applied by two panels of the Court of Appeals and the Kansas Supreme Court.
- When considering the validity of a liquidated damages clause courts apply a ***prospective*** analysis: what could the parties reasonably anticipate at the time of contracting.

30

## Carrothers Construction Co. v. City of South Hutchinson

- Court addresses whether the prospective analysis will be followed by a second analysis which compares the liquidated damages with actual damages: a ***retrospective*** analysis.
- Kansas Supreme Court rejects use of a retrospective analysis to test the validity of a liquidated damages clause.

31

## Carrothers Construction Co. v. City of South Hutchinson

- City contracts with Carrothers to build a $5,618.00 sewage treatment plant.
- Contract includes a clause imposing $850 per day in liquidated damages for delay in achieving either "substantial completion" or "final completion."
- 170-day delay to "substantial completion."
- 1-day delay to "final completion."

32

## Carrothers Construction Co. v. City of South Hutchinson

- Although City began operating plant in November, "substantial completion" did not occur until January when it could be operated using the new computer system and all the safety systems.
- Also contained a clause allowing the project engineer to determine when the work had reached "completion" as defined in the contract. Acted in good faith.

33

## Carrothers Construction Co. v. City of South Hutchinson

- City withheld $145,350 in liquidated damages from the final purchase price.
- Carrothers argues this was a penalty because it has no relation to the damages the City actually suffered as a result of the delay.
- **Issue: Under these facts, was the liquidated damages clause an unenforceable penalty clause?**

34

## Carrothers Construction Co. v. City of South Hutchinson

- No.
- MKEC Engineering Consultants, Inc. conducted an analysis of how a delay could impact the City and used this analysis to arrive at the $850/day figure.
- Burden of proof on Carrothers.
- Public policy favors advance agreement on damages.

35

## Carrothers Construction Co. v. City of South Hutchinson

- Limitation on agreement: Cannot be used as "security for performance" (a penalty) as opposed to "a sum certain to be paid in lieu of performance" (liquidated damages).
- Not proper to try and encourage performance – by making in financially painful.
- **COMMENT:** Supports the concept of "efficient breach" of contract.

36

## Carrothers Construction Co. v. City of South Hutchinson

- Test for penalty vs. liquidated damages:
- Examine all terms of the agreement and the circumstances ***at the time of contracting*** to determine:
- (1) The damage figure is conscionable in light of the anticipated damages; and
- (2) Damages are not readily determinable.

37

## Carrothers Construction Co. v. City of South Hutchinson

- "The better test, we believe, is to determine the reasonableness of a liquidated damages clause as of the time the contract was executed, not with the benefit of hindsight."
- "[O]ur decision . . . is intended to lay aside any further doubt and embrace a prospective analysis as the sole basis for evaluating a liquidated damages provision in a contract."

38

## Carrothers Construction Co. v. City of South Hutchinson

- Illustration of the prospective analysis:
- Final completion did not occur until operating manuals delivered.
- One-day delay following substantial completion in delivering manuals triggered $850 in liquidated damages.
- Actual damages. $0 ?
- Liquidated damages. $850

39

## Carrothers Construction Co. v. City of South Hutchinson

- Parties unable to readily calculate damages for delay at the time of contracting.
- Engineering firm properly weighed all factors to arrive at a reasonable figure that represented likely loss: $850/day.
- Another consideration: Dealing with a contract to construct public utility service facilities.

40

## Santa Rosa KM Associates v. Principal Life Insurance Co.

- 1991 Eskie borrowed $6,375,000 from Principal to build shopping center.
- 1998 Santa Rosa purchased shopping center; Principal agreed to the transfer and Santa Rosa assumed Eskie's note and mortgage.
- 2005 Santa Rosa sought to prepay the $4,865,142.24 balance due and was informed a "make whole premium" of $1,636,268.96 would have to be paid to Principal.

41

## Santa Rosa KM Associates v. Principal Life Insurance Co.

- The "make whole premium" was included in the agreements with Eskie/Santa Rosa.
- Also contained an attorney fees provision.
- **Issue: Does the prepayment provision violated public policy?**
- Held: No. Reasonable attempt to anticipate interest rate risk. Examine at the time of contracting, not when triggered.

42

## Santa Rosa KM Associates v. Principal Life Insurance Co.

- **COMMENT:** Although no breach involved to trigger a liquidated damages analysis, the Court employs a similar "at the time of contracting" analysis instead of a hindsight analysis.
- Similar temporal analysis used in unconscionability cases. Except for the *Kansas Baptist Convention* case.

43

## Santa Rosa KM Associates v. Principal Life Insurance Co.

- **Issue: Can the lender recover attorney fees?**
- Yes. The post 1994 version of K.S.A. § 58-2312 applies to this case because of the 1998 amendment to substitute Santa Rosa for Eskie.
- Statute authorizing fees not limited to strictly costs of "collection" but includes this action for interpretation.

44

## Double M Construction v. State Corporation Commission

- Double M was the excavation contractor for Double J Pipeline, LLC.
- Pipeline was supposed to identify utilities in the area for Double M.
- Pipeline contacted Kansas One Call but failed to communicate with Double M concerning a delay in marking.
- Double M proceeded and hit a gas line, killed its employee, and damaged property.

45

## Double M Construction v. State Corporation Commission

- The Kansas Corporation Commission assessed a $25,000 penalty against Double D for failing to comply with the Kansas One Call statutes.
- Double D's defense: it had a contract with Pipeline to locate the utilities.
- Held: Double D cannot delegate its statutory obligation to Pipeline.

46

## In re Marriage of Hudson

- Divorce settlement agreement gave William control over the sale of their house and provided: **"Once the marital residence is sold, in the event a deficiency exists with regard to the second mortgage, Husband shall completely satisfy any such deficiency and hold wife harmless therefrom."**

47

## In re Marriage of Hudson

- The second mortgage was the result of Brenda defrauding William's mother out of $150,000 that was used to purchase the house.
- Brenda pled guilty to one count of wire fraud and was ordered to make restitution to William's mother in the amount of $66,000. This was the deficiency remaining once the house had been sold.

48

## In re Marriage of Hudson

- **Issue: Does the settlement agreement require William to hold Brenda harmless from her $66,000 criminal restitution order?**
- Held: Yes.
- Court finds this is an "indemnity agreement" which is governed by the same rules applied to interpret other contracts.

49

## In re Marriage of Hudson

- **COMMENT:** I don't think so. We have a whole body of law that requires indemnity agreements to be clear and construct strictly to limit them to situations "plainly within the language used."
- Arguably this interpretive rule would require express language that contemplated indemnity for losses associated with a criminal restitution claim.

50

## K.S.A. § 16-121

- **COMMENT:** Lets have the Kansas Legislature write the terms of contracts between commercial parties.
- Example of one segment of an industry seeking bargaining power from the Legislature – and getting it.
- Annual event for the Legislature now as other industries seek their help in negotiating their contracts.

51

## K.S.A. § 16-121

- 2004 Version of the Statute: prohibited, as being **"against public policy,"** an **"indemnification provision is a[n] . . . agreement . . . entered into in connection with a construction contract, which requires the indemnitor to indemnify the indemnitee for the indemnitee's negligence . . . ."**

52

## K.S.A. § 16-121

- Other industries initially rushed to the Legislature to have "construction contract" defined to include their activity.
- These industries started to discover the utility of allowing a party to indemnify another party against negligence, strict liability, and statutory liability.
- Some deals cannot get done without it.

53

## K.S.A. § 16-121

- 2008 Amendments reveal four trends:
- (1) Make it clear their industry ***is*** covered by the statute.
- (2) Make it clear their industry ***is not*** covered by the statute.
- (3) Expand or limit the scope of the prohibition in certain cases.
- (4) Express exclusions of certain indemnity topics.

54

## K.S.A. § 16-121

- Definitions define the scope of the law.
- 2008 went from three to ten definitions.
- Add to coverage "motor carrier transportation contract" and "dealer agreement or franchise agreement."
- Distinguish between "mutual" and "unilateral" indemnity obligations.

55

## K.S.A. § 16-121

- Adds a prohibition on indemnity for any "intended acts or omissions."
- Creates real problems for the party who is the "doer" in a venture.
- Subsection (c) expands the indemnity prohibition to insurance.

56

## K.S.A. § 16-121

- The § (d) exemptions:
- Contractor's agreement to provide "general liability insurance."
- Indemnity against "strict liability under environmental laws."
- Certain settlement agreements.
- Insurance and bonds issued by an insurance of bonding company.
- Certain agreements supported by insurance.

57

## K.S.A. § 16-121

- Broadest exemption is at § (d)(5):
- **"[A] separately negotiated provision . . . Whereby the parties mutually agree to a reasonable allocation of risk, if each such provision is: (A) Based on generally accepted industry loss experience; and (B) supported by adequate consideration."**
- **COMMENT:** Litigation magnets.

58

## K.S.A. § 16-121

- Certain choice of forum and choice of law provisions deemed void.
- § (e): **"[T]he laws of the state of Kansas shall apply and govern every contract to be performed in this state. Any litigation, arbitration or other dispute resolution proceeding arising from such contract shall be conducted in this state."**

59

## K.S.A. § 16-121

- Is the scope of § (e) limited to "contracts" that provide for indemnity?
- Does it apply only to the indemnity portion of the contract?
- **COMMENT:** I predict this statute will be used to attack a number of contractual provisions that are not directly related to indemnity.

60

## Pollack v. Crestview County Club

- What do you do when Rodney Dangerfield is a member of your club?
- Club's bylaws determine the process for expelling members.
- Due process claim: no state action; really asking whether the Club followed its bylaws in responding to the complaint.
- These are contract claims, not constitutional claims.

61

## Pollack v. Crestview County Club

- "'The relationship between a social club and its members is one of contract.'. . . The rules, regulations, and bylaws of social clubs generally establish the terms of such contracts."
- Courts will not evaluate what the Club deems to be "unacceptable behavior."
- Concerned only with whether contractual procedures followed. They were here.

62

## Inter-Americas Insurance v. Imaging Solutions Co.

- Inter-Americas contracted with Imaging for development of software, hardware to run the software, installation, and support.
- Dispute over whether Imaging performed.
- It appears Inter-Americas had a change of heart and made it impossible for Imaging to complete performance whereupon Inter-Americas claimed a breach by Imaging and sued for return of payments made.

63

## Inter-Americas Insurance v. Imaging Solutions Co.

- **COMMENT:** Reminds me of a book Professor E. Allan Farnsworth wrote back in 1998 titled: "Changing Your Mind, The Law of Regretted Decisions."
- Trial Court held it was Inter-Americas, not Imaging, that breached the contract by failing to allow Imaging to perform.
- Court of Appeals: affirms but remands to trial court to determine Imaging's damages.

64

## Inter-Americas Insurance v. Imaging Solutions Co.

- Step One: What body of contract law applies to this situation?
- UCC Article 2 or general contract law?
- $35,000 of the $240,000 contract for services; services incidental to the sale of goods so apply UCC Article 2 to the entire contract.

65

## Inter-Americas Insurance v. Imaging Solutions Co.

- **COMMENT:** Although not mentioned by name, the court applies the "predominant factor" test adopted by the Kansas Supreme Court in *Care Display, Inc. v. Didde-Glasser, Inc.*, 225 Kan. 232 (1979).

66

## Inter-Americas Insurance v. Imaging Solutions Co.

- Contract did not specify a time line for performance.
- Remedy: Image obligated to perform within a "reasonable time." UCC 2-309(1).
- UCC 1-204(2) "reasonable time" depends upon the nature, purpose, and circumstances of the required action.
- Image performed within a reasonable time.

67

## Inter-Americas Insurance v. Imaging Solutions Co.

- Inter-Americas breached the contract by failing to give Imaging timely notice of the alleged breach and a reasonable time to cure the breach.
- UCC 2-602(1) dealing with "rejection of goods." Defective performance must be reported to the other party within a reasonable time.

68

## Inter-Americas Insurance v. Imaging Solutions Co.

- UCC 2-508 and the right to cure.
- The buyer's duty to give notice of "rejection," and the seller's ability to cure a defect in performance, are on-going obligations and rights for contracts that contemplate a series of performances.
- **COMMENT:** Note how the mixed goods and services contract expands this on-going obligation.

69

## Inter-Americas Insurance v. Imaging Solutions Co.

- The Court mentions the duty of good faith but fails to discuss or apply it to the facts.
- **COMMENT:** Two contexts here.
- (1) good faith in ***performance*** – the obligation to cooperate so Imaging can perform.
- (2) good faith in ***enforcement*** – notify non-performing party of their nonperformance.

70

## Lewis v. Kansas Production Co.

- 1972: Oil and gas lease granted by landowner; production timely obtained and continues, extending the lease to the present.
- 1994: Oil and gas lease owner divided it by depth, retaining the "shallow" rights (surface to depth of existing production), and conveying to KPC the "deep" rights (those below the depth of existing production).

71

## Lewis v. Kansas Production Co.

- 2004: landowner contracts to sell land to Lewis and in the process demands that KPC release its deep rights.
- Not a demand for development; demand for a release under K.S.A. § 55-201.
- **COMMENT:** K.S.A. § 55-201 applies to situations where the leasehold rights have terminated and the landowner is entitled to a release to clear their title.
- Importance: one-way attorney fees. 55-206.

72

## Lewis v. Kansas Production Co.

- KPC has made no effort to develop its leasehold rights.
- KPC's rights are held by production from the shallow rights owned by the other lessee.
- **COMMENT:** The lease is not divisible, for purposes of the habendum clause, unless it expressly provides for divisibility.

73

## Lewis v. Kansas Production Co.

- 1983: Kansas Legislature passed the Kansas "Deep Horizons" Act to assist landowners in obtaining development of depths below the deepest depth from which production has been obtained.
- Creates a presumption the lessee breached the implied covenant(s)? to explore and develop deeper zones after 15 years of production from shallower zones.

74

## Lewis v. Kansas Production Co.

- Trial court: KPC violated the Act and ordered cancellation as the remedy.
- Court of Appeals: Cancellation is not an available remedy unless landowner made prior demand for development and provided KPC with reasonable time to act.
- KPC given an opportunity to perform before its lease can be terminated for breach of an implied covenant (even a *statutory* implied covenant).

75

## Lewis v. Kansas Production Co.

- **COMMENT:** The Court momentarily stumbles over the difference between the ***property*** remedy associated with "abandonment" and the ***contract*** remedy associated with breach of an implied covenant.
- In Kansas and oil and gas lease creates a *profit à prendre*, an incorporeal hereditament that can be abandoned if there is an intent to abandon.

76

## Chesbro v. Douglas County

- 1972: Fishburn and County agreed on construction of fence placing 10 feet of Fishburn's property on County-side of the fence (which consisted of a large ditch).
- 2004: Chesbro purchased land from Fishburn and sought access to a County road from the fenced area.
- County denied access because Chesbro's land did not abut the road.

77

## Chesbro v. Douglas County

- The issue regarding the road permit depended upon who owned the 10-foot strip of land.
- Trial court: County obtained it by adverse possession.
- Court of Appeals: affirms.
- Chesbro: Fishburn purported to convey and warrant all the land to me; nothing of record to show the County's interest.

78

## Chesbro v. Douglas County

- Apply K.S.A. § 60-503: **"No action shall be maintained against any person for the recovery of real property who has been in open, exclusive and continuous possession of such real property, either under a claim knowingly adverse or under a belief of ownership, for a period of fifteen (15) years."**

79

## Chesbro v. Douglas County

- Two alternative bases for satisfying the traditional "adverse" requirement: "knowingly adverse" claim (meaning a "hostile" holding) or "belief of ownership" (meaning a non-hostile holding).
- **COMMENT:** Court suggests the belief of ownership must be in good faith. What if it isn't? Doesn't it become "knowingly adverse" at that point?

80

## Chesbro v. Douglas County

- County claims under a good faith "belief in ownership" as a result of the fence placement.
- Continuous maintenance of the ditch area by the County for over 15 years.
- "Tacking" applies to new owner but really doesn't matter because the County had obtained ownership prior to Fishburn's sale to Chesbro.

81

## Chesbro v. Douglas County

- The County does not need to file anything to establish its ownership because it is not based upon any deed or other source of title.
- Because County owned the abutting property, and Chesbro did not, County acted properly in denying road access permit which requires ownership of abutting land.

82

## Southern Star Central Gas Pipeline v. Greuel

- 1917: Landowner grants Wichita Pipe Line Company a pipeline easement.
- Southern Star obtained Wichita Pipe Line's rights in the easement and exercised those rights from as early as 1958 until 2007.
- 2007: Greuel buys land; Wichita Pipe Line easement was never recorded. Facts indicate Greuel qualified as a bona fide purchaser without notice.

83

## Southern Star Central Gas Pipeline v. Greuel

- Southern Star asserts it obtained an easement to use the property for pipeline construction and maintenance by prescription from 1958 through 1972.
- Court applies K.S.A. § 60-503 to determine the existence of a prescriptive easement.
- Court finds all the elements have been satisfied by Southern Star.

84

## Southern Star Central Gas Pipeline v. Greuel

- **COMMENT:** The big mystery in this case is how does Southern Star get around the permissive use problem created by the original express easement?
- Although the issue was raised and acknowledged by the court, the opinion does not indicate it analyzed the issue.
- Southern Star's actions were consistent with the permission originally granted by the express easement.

85

## Southern Star Central Gas Pipeline v. Greuel

- **COMMENT:** I think the facts clearly indicate that Southern Star was engaged in a permissive use of the property until 2007. The prescriptive use clock began in 2007 when Greuel asserted the easement was not effective. At that time Southern Star's possession became "adverse" ("hostile" or "belief of ownership"). This means Southern Star has another 14 years to go on its prescriptive easement.

86

## Stroda v. Joice Holdings, LLC

- 1985: Through inheritance ownership of the W½ became divided between Marie (SW¼) and Edmond (NW¼). Edmond was allowed an implied easement over Marie's land to access his land.
- 2003: Stroda owns of NW¼; Joice owns SW¼.

87

## Stroda v. Joice Holdings, LLC

- 2006: Stroda seeks to sell NW¼ for use as a single residence and claims an implied easement across Joice's SW¼ for access to the NW¼ for agricultural purposes (traditional use) but also to access a residence and provide utility service to the residence.
- There had been a residence on the NW¼ at one time, but it has not been occupied since 1957.

88

## Stroda v. Joice Holdings, LLC

- Trial court: implied easement includes right to access residence and lay utilities.
- Kansas Supreme Court: affirms.
- "[A]ssumed that they anticipated such uses as might reasonably be required for a normal development of the dominant tenement." Restatement (First) of Property § 484, comment b.

89

## Stroda v. Joice Holdings, LLC

- Court holds, regarding utilities:
- "We observe that even when the use is reasonable, it must be necessary; the level of necessity required has been found to be less than strict necessity, but more than inconvenience. In our view a lack of utilities to a new house in Kansas goes beyond mere inconvenience and begins to approach the unlivable."

90

## Friess v. Quest Cherokee, LLC

- Quest, before obtaining approval from the landowner, placed a gas pipeline across the land.
- Friess sued seeking a mandatory injunction to have the pipeline removed.
- Trial court granted the injunction.
- Court of Appeals affirms.

91

## Friess v. Quest Cherokee, LLC

- No adequate remedy at law; continuing violation of the landowner's rights.
- Not required to balance the equities.
- Not an innocent act by Quest, but rather a "foolish or negligent" act.
- No authority or reasonable basis to believe it had authority to use the land.

92

## Central Natural Resources, Inc. v. Davis Operating Company

- 1924: Landowners in Southeast Kansas convey to Central's predecessor: **"all coal . . . together with the right to mine and remove same."**
- 2004: Davis obtains oil and gas leases from landowners, drill wells into the coal, and begin producing methane gas from the coal.
- **Issue: Who owns the methane gas found within the coal?**

93

## Central Natural Resources, Inc. v. Davis Operating Company

- Trial court: The landowners own the methane gas within the coal.
- Supreme Court: Affirms. Conveyance of "coal" did not include methane gas within the coal.
- Central argued no reasonable person in 1924 would have expected to retain methane gas within the coal because the coal owner had a statutory duty to ventilate and otherwise destroy the methane gas as part of the mining process.

94

## Central Natural Resources, Inc. v. Davis Operating Company

- Court adopts an opposite presumption that no reasonable person in the grantee's position would expect to purchase a known hazardous substance like methane.

95

## Central Natural Resources, Inc. v. Davis Operating Company

- Court also rejects Central's argument under K.S.A. § 58-2202 which states: **"[E]very conveyance of real estate shall pass all the estate of the grantor therein, unless the intent to pass a less estate shall expressly appear or be necessarily implied in the terms of the grant."**

96

## Central Natural Resources, Inc. v. Davis Operating Company

- Court states 58-2202 does not apply when the deed purports to convey less than all the estate.
- Court states that even if you apply 58-2202 the grant of "coal" does not suggest the grant of "methane."

97

## Central Natural Resources, Inc. v. Davis Operating Company

- **COMMENT:** The Court's analysis places the burden on the grantor in this case to expressly reference methane as part of the grant.
- It appears title examiners in Kansas can now safely conclude that a grant of "coal" will not include methane gas within the coal, unless the grant expressly confers methane ownership on the coal owner.

98

## Johannes v. Idol

- **Issue: Are various tracts of land part of the decedent's estate, or were they effectively conveyed to various grantees before the grantor's death?**
- **Sub-Issue: Were the deeds effectively delivered to the grantees before the grantor's death?**

99

## Johannes v. Idol

- Grantor signed deeds sometime in 1967.
- Each deed contained reservation of a life estate in the grantor.
- Two or the grantees testified the grantor gave the deeds to them in 1967 or 1968; they were placed in a safe deposit box by one of the grantees. Grantor did not have access to the box.

100

## Johannes v. Idol

- Court of Appeals affirms the trial court's finding that the deeds had been delivered to the grantees prior to the grantor's death.
- The critical inquiry: whether "the grantor had a present intent to divest himself or herself of title to the property and vest it in the grantee."
- Reservation of a life estate is also evidence of an intent to presently deliver.

101

## Johannes v. Idol

- Recording is not necessary to have effective delivery.

102

## Transfer-On-Death Deeds

- Delivery to grantee is not necessary to make it valid.
- However, it must be recorded during the grantor's lifetime to be effective.
- Grantee need not know of its existence.
- K.S.A. §§ 59-3501 to 59-3507.

103

## Rector v. Tatham

- Heirs enter into agreement concerning distribution of their mother's estate.
- Mary would convey property to the mother and in return, at mother's death, brother Cliffor and sisters Patricia and Ruth would direct that any remaining funds in the mother's estate be payable to Mary.
- Mother died and assets distributed equally among all the heirs.

104

## Rector v. Tatham

- Trial court dismissed finding the agreement did not meet the formalities imposed by K.S.A. § 59-102(8) regarding family settlement agreements.
- Court of Appeals reverses holding Mary's claim could be supported as an assignment of an expectancy interest and under a promissory estoppel theory.
- Supreme Court affirms Court of Appeals.

105

## Rector v. Tatham

- Court states: An agreement to assign an expectancy is enforceable "as long as the assignments were fair, were supported by consideration, were not induced by fraud, and were clearly indicative of the intention of the parties."
- The petition properly stated claims for assignment of an expectancy and for promissory estoppel.

106

## Rector v. Tatham

- **COMMENT:** Are potential future but contingent benefits as a grantee under a transfer-on-death deed assignable?
- It would appear this is no different from an assignment of an expectancy as an heir.
- In either situation the interest is contingent on the source of the property not changing their mind and on the heir/grantee surviving the grantor.

107

## Rector v. Tatham

- See February 2008 Bar Exam Question 8.

108

## Estate of Draper v. Bank of America, N.A.

- 1967 Clark and Ethel enter into an antenuptial agreement.
- Mutual agreements with Ethel promising to leave 3/4ths of the estate to Clark's sons (by a prior marriage) if Ethel survived Clark.
- 1977 Clark died and left property to Ethel in accordance with their agreement.

109

## Estate of Draper v. Bank of America, N.A.

- Shortly after Clark's death Ethel set up an irrevocable trust giving Ethel income and corpus during her life with the remainder to charities and individuals – but not Clark's sons.
- 1982 Ethel makes a will dividing her estate equally among Clark's sons. Same day creates another irrevocable trust with same beneficiaries as in the 1977 trust.

110

## Estate of Draper v. Bank of America, N.A.

- October 2002 Ethel dies with less than $10,000 in her probate estate. Assets in the two trusts exceed $1 million in value.
- January 2003 Ethel's will admitted to probate.
- December 2003 the executor, one of Clark's sons, sues the trustees and trust beneficiaries seeking to impose a constructive trust on trust assets.

111

## Estate of Draper v. Bank of America, N.A.

- Trial court: grant the constructive trust.
- Court of Appeals: reverses; Ethel complied with the letter of the agreement.
- Supreme Court: reverses Court of Appeals.

112

## Estate of Draper v. Bank of America, N.A.

- Constructive trust issues:
- It is not necessary to prove actual or constructive fraud to qualify for the remedy.
- Any situation where a third party has an equitable duty to convey it to another.
- It is a remedy; must still have an independent basis that creates the duty to convey.

113

## Estate of Draper v. Bank of America, N.A.

- Constructive fraud – action by a person in a confidential relationship, whereby they breach their fiduciary duty.
- A confidential relationship existed between Clark and Ethel as to the disposition of their estates.
- Also a contractual basis for finding a breach of duty – did not comply with the spirit of the obligation.

114

## Estate of Draper v. Bank of America, N.A.

- "[T]he implied duty of good faith and fair dealing applied to Ethel's agreement to leave three-quarters of her estate to Clark's sons. This duty would not allow Ethel to make gifts that are inconsistent with the justified expectations of Clark that his sons would receive three-quarters of the entire estate Ethel enjoyed at the time of her death."

115

## Estate of Draper v. Bank of America, N.A.

- Is the claim barred by K.S.A. § 59-2239(1), the nonclaim statute? **"All demands . . . Against decedent's estate . . . shall be forever barred from payment unless the demand is presented within the later of: (a) four months from the date of first publication of notice . . . or (b) if the identity of the creditor is known or reasonably ascertainable, 30 days after actual notice was given . . . ."**

116

## Estate of Draper v. Bank of America, N.A.

- Clark's sons had a claim as third party beneficiaries to the antenuptial agreement which would have been subject to the nonclaim statute.
- However, here the claim is being made by the executor seeking to collect and marshal the estate assets under K.S.A. § 59-1401. This is not a claim against the estate and is therefore not subject to the 4-month nonclaim period.

117

## Estate of Draper v. Bank of America, N.A.

- When would the basic unjust enrichment claim arise?
- When the assets were transferred to the irrevocable trusts (1977 & 1982)?
- When Ethel died in 2002?
- Court holds it was when Ethel died. This was when she could no longer fulfill her promise and the point in time when the other parties had an equitable duty to return the property.

118

## Nelson v. Nelson

- 1975 property settlement agreement requires husband/father to provide for their two children.
- Remarries 1978 and remains married to second wife until 2003.
- Husband/father makes gifts to second wife which the two children seek to challenge when their father dies.

119

## Nelson v. Nelson

- Father dies with no assets in his estate.
- Suit by children against wife and other recipients of gifts from the father.
- No estate opened in Kansas; no claims filed in Florida where father resided at his death.
- Trial court, Court of Appeals, and Supreme Court: claims barred by nonclaim statute.

120

## Nelson v. Nelson

- Children needed to open an estate proceeding in a timely manner and then file a claim in a timely manner.
- They did neither so their claims are barred.

121

## In re Estate of Seth

- Laryl Seth is the beneficiary of a will in which his mother left him the 320-acre farm.
- Laryl took the will, in a timely manner, to his attorney to have it probated.
- Attorney failed to act and missed the 6-moth deadline for seeking probate.
- Laryl argued he was an "innocent beneficiary" under K.S.A. § 59-618.

122

## In re Estate of Seth

- See outline, at page 65, for the relevant statutes.
- Laryl will get only 1/3rd of the farm unless the will is admitted to probate.
- The attorney has no insurance and is judgment proof (why should this matter?).

123

## In re Estate of Seth

- **COMMENT:** Court employs some benevolent interpretation to find that Laryl was entitled to the "innocent beneficiary" exception to the 6-month rule.
- Wasn't possession and knowledge by Laryl's agent, the attorney, the same as possession and knowledge by Laryl?

124

## Mangels v. Cornell

- 1996: Bud and Thelma enter into a revocable trust.
- 2004: Bud dies in March and later in the year Thelma amends the trust to favor one of the beneficiaries with $1 million more than they would get under the 1996 trust.
- **Issue: Can Thelma unilaterally amend the trust?**

125

## Mangels v. Cornell

- Court analyzes all the language within the trust instrument and concludes it is joint, mutual, and contractual, and therefore could not be changed by Thelma after Bud's death.

126

## In re Estate of Lane

- Stepmom determined that a farm in her sole name, which she had been awarded in a divorce from her former husband, should not be include in here husband's estate.
- Stepmom determined only one-half the value of cattle and equipment used to run a ranch should be included in husband's estate because of her contribution of labor and payments made from their joint bank account.

127

## In re Estate of Lane

- Trial court awarded stepmom a $35,000 spousal allowance plus a $35,000 homestead allowance.
- Oil and gas royalties and cell phone tower rents associated with stepmom's farm are part of her farm and therefore not part of the estate.

128

## In re Estate of Lane

- Court of Appeals concludes the stepmom properly allocated the assets between her and her deceased husband.
- Also concludes the trial court did not abuse its discretion in awarding the maximum spousal allowance under K.S.A. § 59-403 (outline page 72); the homestead allowance under K.S.A. § 59-6a215 (outline page 73) was proper regardless of her individual ownership of a home.

129

## Frick Farm Properties v. Kansas Department of Agriculture

- Failure to use water right for 5 years empowers Division of Water Resources to terminate the right for nonuse.
- Water rights are statutory real property rights. K.S.A. § 82a-701(g), see Outline page 74.
- Conditions on water right. K.S.A. § 82a-718(a), see Outline page 75.

130

## Frick Farm Properties v. Kansas Department of Agriculture

- Court concludes the DWR followed the proper termination procedures and because Frick failed to present any "due and sufficient cause for nonuse," his water right was properly terminated.

131

## Frank v. Kansas Department of Agriculture

- Frank obtained a permit from the Division of Water Resources to build a "groundwater pit."
- As a condition for issuance of the permit Frank had to build an embankment to keep surface runoff out of the pit.
- When Frank built the embankment, it altered the flow of surface water which caused his neighbor to complain.

132

## Frank v. Kansas Department of Agriculture

- The DWR indicated this situation triggered another condition of the permit that Frank not obstruct a "stream."
- K.S.A. § 82a-301(a) prohibits construction which can "change or diminish the course, current, or cross section of any stream within the state."
- Definition: K.A.R. § 5-40-1(k). Outline at page 76.

133

## Frank v. Kansas Department of Agriculture

- The presumption at issue: See Outline at page 77.
- The court concludes the DWR proved there had been a "stream" at this location so Frank must comply with the regulation.
- **COMMENT:** The court never really addresses the validity of the presumption because it concludes there was, in fact, a stream at the location.

134