In the Zone

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Subsurface Rights and Turn of the (20th) Century Tax Rolls – The Case of *Herder Spring Hunting Club v. Keller*

By Michael J. Kornacki

In *Herder Spring Hunting Club v. Keller* (---A.3d---, 2014 WL 1873877 (Pa.Super.)), the Superior Court of Pennsylvania granted summary judgment to Herder Spring Hunting Club (Herder) in a quiet title action against the heirs of Harry and Anna Keller (the Kellers) and awarded to Herder subsurface rights in a parcel of ground located in Centre County, Pennsylvania, despite the fact that the chain of title contained an express reservation in the Kellers of subsurface and mineral rights in the property. How the court came to that result illustrates the sometime arcane nature of real estate law.

History

In 1894, the Kellers acquired the "Eleanor Siddons Warrant," a tract of land in Centre County, PA containing 460 acres (the Property), at a tax sale. The property was "unseated," meaning it was unoccupied and unimproved (as opposed to "seated" land, which contained permanent improvements.) On June 20, 1899, the Kellers conveyed the surface rights to the property, but in the deed reserved for themselves and their heirs and assigns all subsurface rights in the property.

The surface rights in the property were transferred a number of times until, in 1935, the property was offered for sale by the County Treasurer at a tax sale. Since no bidder offered the upset price, the treasurer conveyed the property to the Centre County Commissioners. The property was still unseated. In 1941, the Centre County Commissioners sold the property to Max Herr, who died intestate in 1944.

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In 1959, Herder acquired the property from Herr's widow. A title search was done at the time, and the Kellers' reservation of subsurface rights was discovered. The deed to Herder contained a statement that "this conveyance is subject to all exceptions and reservations as are contained in the chain of title."

It was recently determined that the property contains shale rich in natural gas. This discovery prompted Herder to file a quiet title action, seeking title to the subsurface rights. In 2010, the trial court in the quiet title action granted to the Kellers' heirs summary judgment, ruling that the reservation of rights was recorded and Herder was aware of the reservation. Herder appealed.

The Appeal

The Superior Court started by noting that a grant of summary judgment will only be reversed "where it is established that the court committed an error of law or abused its discretion." The Superior Court then went on to analyze the history of the property to determine if the trial court correctly applied the law. Surprisingly, the Superior Court's ultimate ruling depended on the interpretation of an old law – §1 of Act of 1806, March 28, P.L. 644, later retitled 72 P.S. §5020-409 (the Act) – which is no longer in effect.

The Act, in relevant part, provided that parties that acquired unseated land were obligated to give to the commissioners or the board for assessment and revision of taxes a statement describing the property so acquired, as well as information relating to the transfer. The purpose of this requirement was to allow for the proper levy of a tax assessment on the unseated property (in contrast, seated land contained permanent improvements that would arguably provide to the commissioners or assessor notice of what party was responsible for taxes). Unfortunately for the Kellers' heirs, it was determined that the Kellers never gave the commissioners notice that the subsurface rights had been severed from the surface rights in 1899, as required by the Act. This would prove fatal to their claim to the subsurface rights in the property.

Although the Act itself did not expressly address situations where subsurface rights were severed from surface rights, the Superior Court reviewed a number of cases that involved both the "horizontal" severance of property (i.e., dividing the property into separate lots) and the "vertical" severance of property (i.e., separation of surface rights from subsurface rights), and reviewed what happened when parties failed to comply with the Act and the properties were subsequently sold at tax sales. The Superior Court found that in those cases, the failure to comply with the Act meant that the tax assessment was levied "*against the property as a whole*," and the tax sale was thus a sale of the entire estate. In situations where the commissioners were not notified of a severance, the tax laws would treat the properties at issue as set forth in their original "warrants" (i.e., the original grants, before severance), and tax them as a whole. For example, in *Hutchison v. Kline*, 49 A. 312 (Pa. 1901), the Pennsylvania Supreme Court ruled that both surface and subsurface rights to a parcel of land should be awarded to a tax purchaser, even though the estates had been severed, because the commissioners were not notified of the severance. The Supreme Court stated "the property had been taxed as a whole, therefore the property was sold as a whole."

And what of the fact that the public record showed that the surface and subsurface estates had been severed, and that Herder had actual knowledge of the

severance? The fact of public recording was of no relevance to the commissioners and assessors – in *Hutchison*, the Supreme Court stated that "the record of the deed creating a separate estate in the minerals would not be notice to the assessor or the commissioners, as they were not bound to search or examine the records." As for Herder, even though its deed specifically referenced "exceptions and reservations as are contained in the chain of title," the Superior Court ruled that "there were no active exceptions or reservations in the chain of title, the horizontal severance having been extinguished" by the 1935 tax sale.

Since the Kellers never informed the commissioners of their reservation of subsurface rights in 1899, the property continued to be taxed as a whole, the treasurer acquired the property a whole, and the treasurer conveyed the property to the commissioners as a whole. The Superior Court thus vacated the award of summary judgment in favor of the Kellers' heirs, and remanded the case back to the trial court to enter summary judgment in favor of Herder.

The recent boom in natural gas exploration in Pennsylvania has given rise to complex questions regarding subsurface rights. Sometimes we are required to look deep into the past to answer these questions.

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Legislative Update in Pennsylvania

By David H. Comer

House Bill No. 1052 proposes to amend the Pennsylvania Municipalities Planning Code (MPC) by expanding the ways by which a municipality is permitted to use the recreational fees it collects in connection with subdivision and land development projects.

Currently, Section 503(11)(iii) of the MPC states the following: "The subdivision and land development ordinance may include, but need not be limited to: (11) Provisions requiring the public dedication of land suitable for the use intended; and, upon agreement with the applicant or developer, the construction of recreational facilities, the payment of fees in lieu thereof, the private reservation of the land, or a combination, for park or recreation purposes as a condition precedent to final plan approval, provided that: (iii) The land or fees, or combination thereof, are to be used only for the purpose of providing park or recreational facilities accessible to the development."

The proposed legislation would expand the potential uses for the fees by providing that the fees could be used for the purpose of providing AND acquiring, operating or maintaining park or recreational facilities reasonably accessible to the development.

Representative Robert Freeman, who serves the 136th Legislative District in Northampton County, PA, was a co-sponsor of House Bill No. 1052. In a memorandum summarizing the proposed legislation, Freeman provides the following explanation: "Currently, the Section 503 of MPC only allows fees incurred from payment in lieu of recreational facilities to be used only for the purpose of providing park or recreational facilities accessible to the development. Fees may only be used for costs incurred to construct the specific recreational facilities for which the fees were collected. My legislation would remove the language found in Section 503 that requires these fees to be used for the specific recreation facilities for which the fees were collected, and will permit municipalities to utilize these funds not only for providing, but also operating or simply maintaining park or recreational facilities anywhere within the municipality."

As for the status of House Bill No. 1052, it has not yet been signed into law; it has passed in the House and is under consideration in the Senate.

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Update on New Jersey Economic Opportunity Legislation

By Jeffrey M. Hall

The tweaking of the New Jersey Economic Opportunity Act of 2013 resumed in earnest in May after the legislative recess. As reported in the March and April issues of *In the Zone*, bills introduced by Senator Raymond Lesniak received Senate Committee scrutiny. The Economic Opportunity Act of 2014, Part III, which, among other things, seeks to correct errors in the Act continue to advance in both houses. In late May, a Senate Committee passed S1551. This bill makes several technical changes to the Act the most notable being the extension of the date by which a developer must obtain a temporary certificate of occupancy for the project. It proposes to extend the date from July 28, 2015 to July 28, 2018, a full three-year extension. For other changes, please see previous editions of *In the Zone*.

The Assembly version of the same bill, A3213, advanced through Committee in early June. The same three-year extension from July 28, 2015 to July 28, 2018 is included in this bill. This extension will allow a developer seeking tax credits under the ERG program the additional time to submit a temporary certificate of occupancy for the project. While passage of some of the legislation has been doubted by some, it is expected that the technical amendment extending the time in which to submit a temporary certificate of occupancy will pass in present form or amended form. On June 23, A3213 was voted to the floor by the Assembly Appropriations Committee and on June 24, S1551 received similarly favorable treatment from the Senate Committee. he Legislature settled on A3213 which passed the Senate 35 to 3 and the Assembly 53 to 18 (6 abstentions) on June 26th. Now in the hands of Governor Christie, a conditional veto with proposed changes is anticipated as it is widely believed that the Governor is not in favor of the bill in its present form.

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Pennsylvania Commonwealth Court Finds that a Homeowners Association is Intended Third-Party Beneficiary of Development Agreement with Right To Enforce its Terms

By Kimberly A. Freimuth

In the case of *College Woods Homeowners Association v. Trappe Borough,* 2014 WL 3056140 (July 7, 2014), College Woods Homeowners Association (Association) filed a contract action against Trappe Borough (Borough) seeking to compel the Borough to take dedication of two streets within the residential development. The Association argued that it was an intended third party beneficiary with standing to enforce a Subdivision and Development Agreement between the Borough and the developer of the residential subdivision (the Agreement).

By way of background, after the developer had completed construction of the roads and other public improvements within the development, the borough engineer confirmed that the improvements had been completed in compliance with the relevant Borough requirements and the Agreement. Yet, despite the developer's request, the Borough refused to release the developer's escrow until the developer sued the Borough, at which point the escrow was released, but the streets were never accepted for dedication by the Borough. Four years later, the Association sent a letter to the Borough requesting that the Borough accept dedication of the streets, but the Borough did not agree to accepted dedication. As a result, the Association filed a complaint claiming that the Borough had a contractual obligation pursuant to the Agreement to accept dedication of the streets within the development. After both the Association and the Borough filed motions for summary judgment, the trial court granted the Borough's motion, determining that there were no material facts in dispute and holding that the Association was not an intended third party beneficiary to the Agreement and, as a result, had no standing to enforce the Agreement. The trial court also held that the Agreement did not impose an obligation on the Borough to accept dedication of the streets.

Thereafter, the Association filed the subject appeal with the Pennsylvania Commonwealth Court, arguing that it was an intended third party beneficiary with standing to enforce the Agreement and further arguing that the Agreement imposed a duty on the Borough to accept dedication of the streets.

In determining whether the Association was a third party beneficiary of the Agreement, the Commonwealth Court cited the Pennsylvania Supreme Court's decision in Guy v. Liederbach, 459 A.2d 744 (Pa. 1983), noting that such a determination requires a two part test: "(1) the recognition of the beneficiary's right must be 'appropriate to effectuate the intention of the parties', and (2) the performance must 'satisfy an obligation of the promisee to pay money to the beneficiary' or 'the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.'"

The court then noted that the first part of the test sets forth a standing requirement which leaves discretion with the court to determine whether recognition of third party beneficiary status would be appropriate. Because the court concluded that the Agreement contained a promise by the Borough to the developer to accept dedication of the streets, the court deemed that, in order to appropriately effectuate the parties' intention, the Association's right to enforce that promise should be recognized. The court appropriately noted that, until the streets are accepted for dedication by the Borough, the Association has the obligation to maintain those streets, thereby further confirming the Association's status as the main beneficiary of the promise.

The second prong of the test required the court to determine whether the circumstances indicated that the developer intended to give the Association the benefit of the Borough's promise to accept dedication of the streets. The court held that the Association is the only party with an interest in enforcing the Borough's obligation to accept dedication of the streets since the developer's escrow had been released. Further, in looking at the provisions of the Agreement itself, the court found that the Agreement

evidenced an intention to benefit not only the developer and the Borough, but also potential purchases of properties in the development, such as the Association's members.

In finding that both prongs of the test were met, the court, in an unreported decision, reversed the decision of the trial court and held that the Association was an intended third party beneficiary to the Agreement with the right to enforce the Agreement.

Yet the court did not stop there. The court went on to address whether the Association could establish that the Agreement imposed a duty on the Borough to accept dedication of the streets. In holding that the Agreement did impose such a duty on the Borough, the court noted that the Agreement contained multiple instances of language requiring or contemplating the offer of dedication of public improvements to the Borough and language assuming the Borough's acceptance of such offer. Specifically, the Agreement contained language requiring the developer to complete the improvements and receive approval from the Borough Engineer for the improvements, which improvements would then be offered to the Borough for dedication and, so long as the requirements of the Agreement had been met, the Borough would accept dedication. Given these provisions, the court held that it was the intention of the parties not only for the developer to offer the streets for dedication, but also for the Borough to accept dedication once the terms of the Agreement had been met.

Although this was an unreported decision of the Commonwealth Court, it is telling of where the court stands on matters of dedication. Based on this case, if the agreement between the developer and the municipality contains language indicating that certain public improvements are proposed to be offered for dedication upon completion in accordance with the municipality's standards, such language will be construed as an assumption that the municipality has agreed to accept dedication of such improvements. Further, the homeowners with the development will become third party beneficiaries of the assumption of acceptance of dedication and will have the ultimate right to enforce such dedication.

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Transactions

David Restaino and John Grossman recently succeeded in being granted, on behalf of an institutional client, an adjudicatory hearing by the NJ Department of Environmental Protection (DEP) on our petition arising from the DEP's denial of a final, environmental permit application, for remedial action for groundwater, recommended by our client's Licensed Site Remediation Professional (LSRP). They contended, among other things, that no authority exists under the LSRP program for such a denial. Additionally, there is no NJ Administrative Code provision in place governing such a petition or providing the parameters for the grant or denial of an adjudicatory hearing request under these circumstances. This was one of the first adjudicatory hearing requests granted by the NJDEP with regard to one of these permits.

On behalf of his client, Daniel V. Madrid closed on a $2.1 million dollar purchase of vacant land in the Journal Square neighborhood of Jersey City, New Jersey. The client, a foreign-capital backed real estate investment company, intends to construct a mixed-use project consisting of commercial/retail space and twenty four residential condominium units.

Jeffrey M. Hall recently assisted The Salvation Army in the closing of Phase 2 of the acquisition of a 25 acre site from the City of Camden Redevelopment Agency for the Ray and Joan Kroc Camden Corps Community Center. Phase 2 will be dedicated to active recreational use. The Kroc Center is a 125,000 square foot Community Center constructed on a closed contaminated landfill. Fox Rothschild assisted with the various aspects of the project including revisions to the redevelopment plan and agreement, zoning changes, planning board approvals, environmental, acquisition, and tax credits.