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In the Zone

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Fee Awards and the Prevailing Party

By John L. Grossman

Clients often ask whether they are entitled to an award of attorneys' fees in bringing or defending a particular cause of action. Unless provided for by agreement, by statute or by court rule, the answer is generally "No." One rule does permit an award of fees, at a court's discretion, to a party seeking to enforce a court order. The party must be a "prevailing" party to entitle it to an award. However, to be "prevailing," a party does not have to be entirely successful.

In *Malden Real Estate v. Cycle Craft, Inc.*, decided in early January 2012, the Appellate Division of the Superior Court of New Jersey awarded a commercial tenant attorneys' fees, even though the tenant did not succeed on all of its claims against its landlord. New Jersey courts have adopted a two-prong test to determine the prevailing party in a civil action. First, the party must demonstrate that the action was causally related to securing the relief obtained; a fee award is justified if a party's efforts are a necessary and important factor in obtaining the relief. The second prong requires a party to establish that the relief granted had some basis in law. A party may be considered prevailing, even though a final judgment may not have been entered in that party's favor, so long as the party has won substantially the relief originally sought in its complaint.

In this case, a shopping center tenant purchased its business from a predecessor and assumed an existing lease. Shortly thereafter, and under the doctrine of eminent domain, the state condemned a portion of the center for road widening purposes and paid the landlord approximately $650,000 as compensation. This resulted in the elimination of several parking spaces used by the tenant's business and affected access to the area of the center directly in front of the tenant's business. The tenant initially sued the landlord, alleging breach of its lease and seeking damages resulting from both the elimination of the parking spaces and the negative impact on its business caused by the road project. The parties settled, providing for the landlord to pay the tenant approximately $15,000 and to reduce the tenant's rent on a monthly basis. The settlement was memorialized in a court order.

The problems continued. Several years later, the landlord sued the tenant for unpaid rent and common area maintenance (CAM) charges, both of which had been withheld by the tenant. The tenant counterclaimed, alleging breach of the settlement agreement, breach of the implied covenant of good faith and fair dealing, and a violation of the New Jersey Consumer Fraud Act. The trial judge found the landlord had breached the terms of the settlement agreement and the implied covenant of good faith and fair dealing; the lower court awarded the tenant a retroactive rent abatement but determined the tenant owed the landlord for unpaid CAM charges. That court also dismissed the tenant's Consumer Fraud Act claim. Finally, the trial judge denied both parties' demands for attorneys' fees.

Although the tenant was required to pay the landlord the balance of the CAM charges it had withheld, the tenant prevailed on its claimed breach of the settlement agreement. The Appellate Division concluded the tenant should be considered the prevailing party on the breach of settlement claim, which was supported by the lower court's award of damages to the tenant in overcharged rent to offset the unpaid CAM charges. The court found the tenant's counterclaim was necessary to enforce the terms of the settlement agreement and to secure relief from the landlord's excessive rent charges, thus satisfying the first prong of the two-prong test. The tenant met the second prong because the trial judge granted the relief of rent abatement pursuant to the settlement agreement. Buttressing that determination was the trial judge's finding that the landlord did not act in good faith in attempting to remedy the traffic issues caused by the construction project. Accordingly, while the tenant did not prevail on all its claims, it did prevail on its claims to enforce the settlement agreement and therefore was entitled to a fee award.

While not necessarily a topic of this article, the Appellate Division upheld the trial judge's finding that the New Jersey Consumer Fraud Act did not apply to the tenant's claims. While the landlord may have breached the terms of its settlement agreement, no aggravating circumstances were found to exist in that breach; substantial aggravating circumstances must be present in addition to the breach to trigger an award under the Consumer Fraud Act.

This case confirms that fee awards may be had, even in circumstances in which the disposition of a dispute does not result in complete victory.

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Landlords: Beware When Terminating and Evicting Commercial Tenants

By Brian J. Levin

When a tenant under a commercial lease defaults and the landlord wishes to exercise a right to terminate the lease and evict the tenant, the landlord must comply with the terms of the lease and the applicable law regarding termination and eviction. This issue was addressed in a September 8, 2011, decision by the U.S. Bankruptcy Court for the Eastern District of Pennsylvania, which held the landlord failed to comply with the prerequisites for evicting a tenant under the Landlord-Tenant Act of 1951, and as a result, the lease was not terminated and the landlord was not entitled to have the debtors evicted from the premises (See *In re Ice Treats One, Inc.*)

In the case in question, the tenant, operating as a Rita's Water Ice, failed to timely pay its rent to the landlord. The landlord sent a letter to the tenant indicating the tenant would be in default if it failed to make the required payment within 10 days of the date of the letter. Two days after sending the default letter, the landlord, without notifying the tenant, filed a landlord-tenant complaint in the Philadelphia Municipal Court against the tenant. Upon expiration of the 10-day cure period, the landlord sent the tenant a letter terminating the lease and demanding the tenant vacate the premises within 15 days. The Municipal Court granted judgment against the tenant and the landlord ultimately took possession of the leased premises and installed a new operator. The tenant filed a petition to open the default judgment, and the Municipal Court vacated the judgment but issued a new judgment for possession and a monetary judgment in favor of the landlord. In the tenant's appeal to the Court of Common Pleas, it filed a suggestion of bankruptcy, the intent of which is to notify a court that the defendant has filed a bankruptcy petition. The filing of a bankruptcy petition operates as an automatic stay of any act to exercise control over property of the estate.

The issue at hand for the Bankruptcy Court was whether the tenant, as the debtor, was entitled to the protection of the automatic stay. To make such a determination, the court first had to determine if the lease had been terminated by the landlord prior to the date on which the tenant filed its bankruptcy petition. If the lease was not terminated prior to the bankruptcy filing, then the filing would operate as an automatic stay of the landlord's right to evict the tenant and take back possession of the leased premises. In its analysis of the Landlord-Tenant Act of 1951, the court found that 68 P.S. §250.501 required that a landlord must give a tenant a notice to quit **before** commencing eviction proceedings in order to effectively terminate the lease and evict the tenant. In the case before the court, the notice sent by the landlord to the tenant before the landlord commenced eviction proceedings was a default notice, not a termination notice (or notice to quit). The landlord's termination notice was sent after the landlord commenced eviction proceedings. As a result, the landlord failed to comply with the prerequisites for commencing its eviction proceedings and thus the judgments against the tenant should not have been granted by the Municipal Court and the landlord was not entitled to have the tenant evicted from the premises. As the landlord did not effectively terminate the lease, the tenant's bankruptcy petition entitled the tenant to retain its interest in the lease and the protection of the automatic stay. Based upon the court's findings, the tenant, as the debtor, could assume the lease (if it so chooses), provided it complies with the requirements of Section 365 of the Bankruptcy Code.

This decision points out the importance of reviewing and understanding the requirements, both in the applicable lease and the law, to affect a proper termination of a commercial lease. Had the landlord proceeded properly and in compliance with the lease and the Landlord-Tenant Act, the lease could have been terminated and would not have been subject to the protection of the automatic stay.

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Legislative Update in Pennsylvania

By David H. Comer

House Bill No. 1484 proposes to amend the Pennsylvania Municipalities Planning Code (MPC) by adding a definition of a new term, "mailed notice," and providing a mechanism by which landowners and owners of a mineral interest in land can obtain notice of various public hearings.

First, the proposed legislation would add the following definition of "mailed notice" to the MPC: "**[N]otice given by a municipality by first class mail to a landowner or an owner of a mineral interest in land of the time and place of a public hearing and the particular nature of the matter to be considered at the hearing**." It is interesting to note the proposed definition does not only include landowners but also includes owners of a mineral interest in land.

Mailed notice would be required by the MPC based on the proposed legislation

only when a landowner or an owner of a mineral interest in land within a municipality has made a request that the notice be mailed and has supplied the municipality with a stamped, self-addressed envelope prior to the public hearing.

The proposed legislation would require the governing body hold public hearings pursuant to public notice **and** mailed notice in situations involving (1) adoption of the official map and amendments thereto, (2) enactment of subdivision and land development ordinances and/or amendments and (3) enactment of zoning ordinances and/or amendments.

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Does the Surface Mining Reclamation Act Preempt Local Zoning Establishing Setback Requirements Greater Than Contained in the Act?

By Herbert K. Sudfeld, Jr.

In *Hoffman Mining Company, Inc. v. Zoning Hearing Board of Adams Township, Cambria County and Township of Adams*, 2011 WL 5865672 (Pa.), the Pennsylvania Supreme Court affirmed the decision of the Commonwealth Court on the question whether the Surface Mining Conservation and Reclamation Act (Surface Mining Act) preempted a provision in a local zoning ordinance that established a setback from all residential structures that was greater than the setback provisions of the Surface Mining Act. The Supreme Court held the local zoning provision was not preempted and affirmed the order of the Commonwealth Court.

In this case, the local provision required all mining, excavating and blasting activities to maintain a 1000-foot setback from all residential structures. The Surface Mining Act provided that the setback should be 300 feet from an occupied dwelling and had a preemption clause that read:

> "Except with respect to ordinances adopted pursuant to the … "Pennsylvania Municipalities Planning Code," [53 P.S. § 10101 et seq.,] all local ordinances and enactments purporting to regulate surface mining are hereby superseded. The Commonwealth by this enactment hereby preempts the regulation of surface mining as herein defined."

The court stated that "absent a clear statement of legislative intent to preempt, state legislation will not generally preempt local legislation on the same issue." In deciding whether the Surface Mining Act preempted the local setback provision, the court noted there are three types of preemption:

> "(1) express or explicit preemption, where the statute includes a preemption clause, the language of which specifically bars local authorities from acting on a particular subject matter; (2) conflict preemption, where the local enactment irreconcilably conflicts with or stands as an obstacle to the execution of the full purposes of the statute; and (3) field preemption, where analysis of the entire statute reveals the General Assembly's implicit intent to occupy the field completely and to permit no local enactments."

The court provided an in-depth analysis of the two regulations as well as recent case law on the subject and determined the Surface Mining Act's preemption clause does not expressly preempt local regulation of land via zoning ordinances, which may affect where surface mining is located or sited, stating the regulation here does not regulate surface mining as that term is defined in the Act. Rather the provision falls within the purview of standard zoning regulation.

The court further held that conflict preemption exists where the local ordinance cannot be sustained to the extent that it is contradictory to or inconsistent with the state statute and is therefore irreconcilable. However, no such conflict preemption exists in the instant case as the local ordinance provides no obstacle to the execution of the statutory purposes of the Act.

In the area of field preemption, the court likewise concluded the General Assembly did not intend for the Surface Mining Act to be exclusive with respect to the siting or location of surface mining in a municipality.

This holding is consistent with the court's recent decision in *Huntley & Huntley, Inc. v. Borough Council of Oakmont*, 600 Pa. 207, 964 A.2d 855 (PA2009), wherein the court held the express preemption clause of the Oil and Gas Act did not preempt a local zoning ordinance that barred drilling in certain areas of the township.

It should be noted that both the House and Senate of the Pennsylvania legislature are currently considering legislation that will absolutely restrict a local municipality from enacting zoning ordinance provisions in contradiction of the Oil and Gas Act, thereby providing a complete preemption of the Act over local regulation.

For more information, please contact Herbert K. Sudfeld, Jr. at 215.918.3570 or hsudfeld@foxrothschild.com.

Groups Petition To Redesignate the Delaware River as an Exceptional Value

By Robert W. Gundlach, Jr.

The Delaware Riverkeeper Network, American Rivers, Clean Water Action, Pennsylvania Council of Trout Unlimited and more than 20 local, state and national organizations are submitting a stream upgrade petition to the Pennsylvania Department of Environmental Protection (PADEP) to urge the Commonwealth to redesignate to "Exceptional Value" status the Upper and Middle Delaware River and all tributary streams flowing into the river in these reaches on the Pennsylvania side.

This designation is reserved for the cleanest streams of the Commonwealth, and only about four percent, or 3,076 miles of Pennsylvania's 86,000 miles of streams, have received this designation, according to 2009 data. Many of the streams of the proposed upgrade area have already received a "High Quality" designation. The petitioners are submitting a 70-plus page petition that highlights water quality data from agency and nonagency sources and other qualifiers that they say make this watershed deserving of an upgrade to Exceptional Value - the highest designation available to Pennsylvania streams. With this designation should come stronger protections to ensure this region's water quality does not degrade in health over time.

The Upper and Middle Delaware segments extend from the New York border down to Water Gap, PA. The Lower Delaware, which is not the subject of the petition, flows from Water Gap, PA to Trenton, NJ, and, the balance of the river to Philadelphia is considered tidal.

According to the petitioners, the current designation given to the Upper and Middle Delaware and its tributaries do not reflect the unique and important attributes of this river region as a whole. They are requesting the PADEP expedite the petition due to proposed drilling in Marcellus Shale deposits anticipated for the region, which is underlain by the Marcellus Shale.

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Condo Developments Must Reapply for FHA-Insured Loans

By Carrie B. Nase

Following the economic collapse of 2008, many aspects of the home financing system have significantly changed. Whereas it was once relatively simple for a condominium developer to qualify a potential buyer with excellent credit, changes to down deposit requirements have made it a more challenging proposition. Previously, when the condo buyer could not place 20 percent down, options had existed through private mortgage insurance companies to help bridge the difference. However, those past options no longer exist.

Alternatively, if a condominium development is approved by the Federal Housing Administration, potential condo buyers can obtain FHA-insured loans that include lower down deposit requirements, thereby facilitating the sale of condo units.

FHA guidelines state, "To be eligible for FHA mortgage insurance, the project must have been declared and exists in full compliance with applicable state law requirements of the jurisdiction in which the condominium project is located and with all other applicable laws and regulations."

Rules to the FHA-approval process for condominium developments have been changed. The possibility of spot loan approval for individual units was eliminated in 2010 in favor of project-wide approval. And, the FHA now requires FHA-approved condominium developments to seek recertification every two years to maintain FHA-insured financing. That process must begin six months prior to the current approval's expiration.

Current condominium developers and associations can visit the HUD web site to determine whether their communities are currently FHA-approved projects.

Failure to recertify with FHA within the deadline will result in the developer losing its FHA-insured lending status and reverting to more stringent lending standards. While the community can reapply, such new applications will be subjected to a longer and more detailed review versus simply extending a condominium's existing qualifications.

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Case Summary: *1982 East, LLC v. Commissioner of Internal Revenue*

By Jerald David August and Ricardo A. Antaramian

The U.S. Tax Court, in *1982 East, LLC v. Commissioner of Internal Revenue*, T.C. Memo. 2011-84 (2011), again upheld the disallowance of a charitable deduction under section 170 of the Internal Revenue Code for the contribution of a historic preservation easement. Subject to a number of special rules, a taxpayer making a qualified conservation contribution is generally allowed a deduction for any such contribution made during the taxable year. In order for a contribution of real property to qualify under these special rules, the contribution must be: (1) of a qualified real property interest; (2) made to a qualified organization; and (3) exclusively for conservation purposes.

A "qualified real property interest," for purposes of obtaining a deduction under section 170, means either the donor's entire interest in the donated property (except for rights to subsurface minerals and fossil fuels and the rights to access such materials), a remainder interest in the property or a perpetual restriction on the use that may be made of the donated property. Qualified organizations generally include governmental organizations as well as public charities and certain private foundations organized as section 501(c)(3) organizations. While conservation of a certified historic structure qualifies as a conservation purpose, the contribution must be **exclusively** for that purpose. The exclusivity requirement, which mandates the conservation purpose be protected in perpetuity, was the primary issue in *1982 East, LLC*.

The case involved a limited liability company (1982 East, LLC) that claimed a deduction on its 2004 partnership return for the contribution of a historic preservation easement and unused development rights on a five-story townhouse located in the Metropolitan Museum Historic District in New York City. By virtue of its location, any alteration to the building required approval of the New York City Landmarks Preservation Commission. The contribution had been made to the National Architectural Trust (NAT) after the property had been classified by the U.S. Department of the Interior National Park Service as a certified historic structure. A conservation deed of easement was executed, which precluded the LLC and its successors from altering the protected facade of the property (i.e., all exterior surfaces visible from the street level on the opposite side of East 82d Street).

A mortgage loan had originally been used to acquire the property but was ultimately consolidated with a second mortgage that had been obtained to finance the renovation of the property. Because of the conservation easement, the lender was asked to sign and executed an agreement with the taxpayer under which the lender subordinated its rights in the property to NAT's rights to enforce the conservation purpose in perpetuity. Despite the subordination, the IRS denied the deduction for the contribution of the property on the basis that the outstanding mortgage prevented the donated property from being protected in perpetuity, as statutorily required. The taxpayer, on the other hand, argued the subordination was sufficient to protect the conservation purpose of the donated property.

Ultimately, the question addressed by the court was whether the donation complied with the requirement set forth in Treasury Regulation section 1.170A-14(g)(6)—namely, whether NAT would be entitled to a proportionate share of proceeds in the event of a casualty or condemnation occurring before the mortgage on the property would be satisfied. In holding this requirement was not met and upholding the disallowance of the deduction, the Tax Court looked to its prior opinion in *Kaufman v. Commissioner*, 134 T.C. 182 (2010), which it considered to be directly on point.

In *Kaufman*, the court found the organization to which the property was donated **must** be entitled to its proportionate share of future proceeds and demonstrating the mortgage would likely be satisfied was insufficient. As in *Kaufman*, the LLC's lender would be entitled to all condemnation and insurance proceeds by virtue of its prior claim, and NAT would not be entitled to any funds until the mortgage was satisfied. The possibility that NAT would not receive the value dedicated to the conservation easement prior to the mortgage being repaid prevented compliance with the enforceability in perpetuity requirement of Treasury Regulation section 1.170A-14(g)(6)(ii). Also, that a New York court might find the easement unenforceable under New York law was insufficient because NAT's entitlement to the value of the donated property had to be guaranteed.

A corollary issue also addressed by the court was whether a conservation purpose existed as a result of the contribution of the facade easement to NAT. The court found the rights possessed by NAT under the facade easement did nothing to preserve the property. Instead, because the property was located in a historic district subject to local laws and the rules of the New York City Landmarks Preservation Commission, it was those laws and rules that caused the preservation of the property and therefore, the donation did not have a conservation purpose.

1982 East, LLC shows that taxpayers, prior to making a contribution of property for conservation purposes, need to carefully review the requirements, including justified reliance on a bona fide and independent appraisal, that must be met in order to properly claim a corresponding charitable contribution deduction.

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Draft Chesapeake Bay WIP Open for Comments

By Kimberly A. Freimuth

The Pennsylvania Department of Environmental Protection (PADEP) recently released Pennsylvania's Draft Phase 2 Chesapeake Watershed Implementation Plan (draft Phase 2 WIP) as part of its mandated requirement to clean up the Chesapeake Bay. Forty-three counties in Pennsylvania contribute to the Chesapeake Bay watershed.

The draft Phase 2 WIP was submitted to the U.S. Environmental Protection Agency (EPA) on December 15, 2011 – with formal notification appearing in the *PA Bulletin* – and outlines the state's plan to address the EPA's expectations that the states develop a Phase 2 WIP so that local partners (1) are aware of the WIP strategies; (2) understand their contribution to meeting the TMDL allocations; and (3) have been provided with the opportunity to suggest any refinements to the WIP strategies.

The draft Phase 2 WIP was developed to meet the EPA's August 1, 2011, revised nutrient and sediment allocations for the TMDL. The allocations are the result of the EPA's development of a revised watershed model.

According to the EPA's current watershed model, when compared to 1985, Pennsylvania has achieved 27 percent of the nitrogen reductions, 31 percent of the phosphorus reductions and 50 percent of the total suspended sediment reductions needed to reach the 2025 restoration targets. When compared to current 2010 progress reported by the watershed model, Pennsylvania still needs to achieve an additional 33.23 million pound reduction in nitrogen, 1.26 million pound reduction in phosphorus and 524.4 million pound reduction in sediment by 2025 to aid in restoring water quality in the Chesapeake Bay. Failure to meet pollutant contribution reductions in the Chesapeake Bay watershed may result in the EPA tightening limits on permits and/or denying permits outright.

Sen. Mike Brubaker (R-Lancaster) hosted a briefing with the EPA, PADEP and other officials outlining the Commonwealth's draft Phase 2 WIP. (Watch video – click on each speaker name to hear their respective briefings.)

The PADEP is accepting comments from the public on the draft Phase 2 WIP until January 30, 2012.

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The "Grow New Jersey Assistance Program" Is Now Law

By Jeffrey M. Hall and Daniel V. Madrid

In last month's issue, we reported on S3033, which at the time had been passed by both houses of the New Jersey Legislature. On January 5, Governor Christie signed the legislation into law creating the Grow New Jersey Assistance Program. In brief, this legislation encourages capital investment, new job growth and existing job retention by providing businesses with a base $5,000 annual tax credit per job. A qualifying business must make a minimum capital investment of $20 million at an approved location and employ at least 100 employees throughout the 10-year tax credit period.

For detailed information regarding this exciting new tax credit program, please read our alert, "New Jersey's Latest Tool For Economic Growth: The Grow New Jersey Assistance Program" for a thorough breakdown of the law.

In next month's issue, we'll cover A1851. Is it an opportunity lost? Stay tuned for our review of whether New Jersey should revisit legislation creating a state historic tax credit program.

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Chester County Posts Final Draft Stormwater Standards

By Robert W. Gundlach, Jr.

On December 21, 2011, the Chester County Water Resources Authority published the Final Draft of its county-wide Act 167 Stormwater Ordinance Standards Matrix. The Authority has been conducting county-wide Act 167 stormwater planning with county municipalities for the past several years and has integrated its input into the final draft.

The county-wide Act 167 plan intends to cover all watersheds in Chester County that do not already have a PA Act 167 plan approved since 2005. The plan objective is to reduce future flooding impact and improve and protect water quality of the county's streams. It also intends to assist municipalities in addressing stormwater management needs and certain NPDES MS4 requirements.

Phase I of the county-wide planning effort consisted of developing a set of draft stormwater ordinance provisions based on municipal input and feedback and confirmation that the Watersheds Plan fulfills the requirements of Act 167. This initial investigative phase was completed June 30, 2010.

The draft ordinance provisions and model ordinance were further developed and finalized during Phase II. Ultimately, after the completion of Phase II, all municipalities in the county will be required to adopt stormwater ordinance standards that are at least equivalent to the final minimum stormwater design standards in the county-wide 167 Plan.

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May a Nonconforming Structure That Has Been Razed Be Rebuilt on an Existing Nonconforming Foundation?

By Herbert K. Sudfeld, Jr.

In the case of *Scott v. Upper Makefield Township Zoning Hearing Board*, 84 Bucks Co. L. REP. 659 (2011), the Court of Common Pleas of Bucks County (Pennsylvania) found the Zoning Hearing Board of Upper Makefield Township had properly decided to allow the construction of a second story and rebuilding of a residence that was nonconforming as to front and rear setbacks.

In this case, the residence in question had been a one-story structure nonconforming as to both the front yard and rear yard setback requirements of the zoning ordinance. The zoning officer granted permits to the owners to raze the building while retaining the existing foundation and basement. The owners then reconstructed the residence on the same foundation and added a second story while doing so.

The appellants owned property to the rear of the residence and challenged the permits on the basis that the owner had lost the right to rebuild a nonconforming structure once they demolished the old structure. They also challenged the owners' right to add a second story, saying the vertical expansion violated the ordinance.

The court found the zoning ordinance allowed for the extension of a nonconforming structure along existing nonconforming building lines as long as the expansion did not further encroach into the front or rear yard areas so as to be closer to the boundary lines than the existing nonconformity.

The court further held that the addition of the second floor did not violate the zoning ordinance since the second story did not project beyond the building line and did not violate the height restrictions contained in the ordinance.

In addition, since the owner's residence was never changed to a conforming condition, it was allowed to be reconstructed on the existing foundation. The court noted the zoning officer had issued the permits specifically authorizing the razing of the building due to unsafe wall conditions, and the owners had only razed the building in connection with that finding and the granted permits.

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