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# 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 May 28, 2010.

I. BUSINESS LAW

A. Managing Entities and Non-Entities


   a. Mr. Kesler borrows money using a tract of land as collateral.

      (1) 2004 Kesler borrows $50,000 from Landmark National Bank and gives Landmark a first mortgage on a tract of land in Ford County.

      (2) 2005 Kesler borrows $93,100 from Millennia Mortgage Company and gives Millennia a second mortgage covering the same land in Ford County.

      (3) Both mortgages are recorded in Ford County.

   b. Millennia sells its second mortgage.

      (1) Millennia’s rights in the second mortgage are assigned to Sovereign Bank, but the assignment is not recorded in Ford County.

      (2) Instead, Sovereign’s rights are administered privately by an entity known as Mortgage Electronic Registrations Systems, Inc. (“MERS”).
c. April 2006 Kesler files for bankruptcy and names Sovereign as one of his creditors. Kesler’s personal liability under the mortgages is discharged by the bankruptcy court. Once the stay is lifted, the following took place regarding the Ford County property and mortgages:

(1) July 2006 Landmark is allowed to pursue foreclosure of its mortgage and names Kesler and Millennia as parties to the action.

(2) Millennia fails to respond and a default judgment is entered.

(3) The property is sold in October 2006 to third parties for $87,000.

(4) Sovereign, in November 2006, seeks to set aside the foreclosure proceedings because neither it, nor MERS, were notified of the foreclosure action.

(5) January 2007 MERS files a similar motion to set aside the foreclosure action.

(6) Kesler had previously filed a motion to obtain distribution of the funds that were in excess of the $87,000 purchase price required to satisfy Landmark’s $50,000 mortgage debt.

d. The trial court, and the court of appeals, held the foreclosure action, and the trial court’s review and rejection of requests to set aside the foreclosure action, were proper. Therefore, Kesler was entitled to distribution of the surplus proceeds from sale of the mortgaged land; the second mortgagee received no portion of the sales proceeds and its rights were extinguished by the foreclosure.

e. The Kansas Supreme Court affirms noting that Landmark acted properly when it sent notice to Millennia, the “Lender” shown of record and the party expressly designated to receive notice in the mortgage documents.

(1) Although MERS was named as a “nominee” for the Lender, and Lender’s successors and assigns, its legal status under the mortgage documents was nebulous (apparently by design).
MERS' function was to serve as an entity that would facilitate assignments of the mortgage without requiring the assignee to be shown in the Ford County records. MERS would be the clearinghouse where the current assignee of the mortgage could be identified internally.

The problem with the MERS system is it failed to account for Kansas law in two ways:

1. First, it ignored the statutory requirements of the Kansas recording system.

2. Second, it failed to confer on MERS a sufficient property interest in the mortgage to identify it as a mortgagee or otherwise make it an interested party entitled to notice.

The result is assignees of mortgages using the MERS system often may not receive notice of actions that impact their financial interests as the current mortgagee. In this case Millennia received notice as the mortgagee of record but had no interest in the mortgage that would prompt it to participate in the proceeding.

Although MERS asserted a policy argument to support the system it has established, the court noted an equally strong policy of ensuring the mortgagor, and other interested parties like Landmark, are able to readily identify the current mortgage owner through the appropriate county records.


a. Michael Chambers and Patrick T. Hayes, through a corporate entity, Metcalf 2000 Manager Corporation ("Manager Corp."), acted as the manager of the Metcalf Associates–2000, L.L.C. ("Metcalf Associates"). Both Manager Corp. and Metcalf Associates were effectively owned 50/50 by Chambers and Hayes.

b. Chambers and Hayes, as the directors of Manager Corp., were deadlocked on how Manager Corp. should exercise its authority as the managing member of Metcalf Associates.
c. The trial court found, following 10 days of testimony, that Metcalf Associates existed to buy and sell commercial real estate but Chambers, a real estate broker that had the listing on one commercial building, was not seeking to actively market the building because Chambers desired to purchase it at what Hayes thought was a below market price.

d. Although the building, and therefore Metcalf Associates, was generating a profit through rents, the trial court nevertheless held that the LLC was effectively deadlocked because the managing corporation was deadlocked and the business “is suffering or is threatened with irreparable injury because the members . . . are so deadlocked respecting the management of the affairs of the . . . company that the requisite vote for action cannot be obtained and the members are unable to terminate the deadlock.”

(1) The statute for a deadlocked LLC is K.S.A. § 17-76,117(b) and provides:

(b) If the business of the limited liability company is suffering or is threatened with irreparable injury because the members of a limited liability company, or the managers of a limited liability company having more than one manager, are so deadlocked respecting the management of the affairs of the limited liability company that the requisite vote for action cannot be obtained and the members are unable to terminate such deadlock, then any member or members in the aggregate owning at least 25% of the outstanding interests in either capital or profits and losses in the limited liability company may file with the district court a petition stating that such member or members desire to dissolve the limited liability company and to dispose of the assets thereof in accordance with a plan to be agreed upon by the members or as determined by the district court in the absence of such agreement. Such petition shall have attached thereto a copy of a proposed plan of dissolution and distribution and a certificate stating that copies of such petition and plan have been transmitted in writing to all of the other members of the limited liability company at least 30 days before the filing of the petition and that the members having the requisite vote required to cause dissolution under the operating agreement have failed or refused to consent to such plan. Unless a majority in interest of the members (or such other number of members having the requisite vote to cause dissolution as the operating agreement may provide) file with the district court within the time period for the answer date of the petition, an answer and a certificate stating that they have agreed on either the petitioner's plan, or a modification or alternative thereof, then the district court shall order that such limited liability company be dissolved, if the district court determines that such irreparable injury and deadlock exists. In any proceeding under this section, the court may appoint one or more trustees or receivers with all the powers and title of a trustee or receiver appointed under K.S.A. 17-6808, and amendments thereto, to administer and wind up the limited liability company's affairs and
may grant such other relief as the court deems equitable.

(2) The statute for a deadlocked corporation is K.S.A. § 17-6516.

(a) The district court, upon application of any stockholder, may appoint one or more persons to be custodians and, if the corporation is insolvent, to be receivers, of and for any corporation when:

(1) At any meeting held for the election of directors the stockholders are so divided that they have failed to elect successors to directors whose terms have expired or would have expired upon qualification of their successors; or

(2) The business of the corporation is suffering or is threatened with irreparable injury because the directors are so divided respecting the management of the affairs of the corporation that the required vote for action by the board of directors cannot be obtained and the stockholders are unable to terminate this division; or

(3) The corporation has abandoned its business and has failed within a reasonable time to take steps to dissolve, liquidate or distribute its assets.

(b) A custodian appointed under this section shall have all the powers and title of a receiver appointed under K.S.A. 17-6901, but the authority of the custodian is to continue the business of the corporation and not to liquidate its affairs and distribute its assets, except when the court shall otherwise order and except in cases arising under subsection (a)(3) of this section or subsection (a)(2) of K.S.A. 17-7212.

e. The court of appeals affirms the trial court finding that because Manager Corp. was deadlocked, as the manager member of Metcalf Associates, Metcalf Associates was also deadlocked because any action taken by the members to bypass the manager's inability to act required the same 50/50 Chambers/Hayes consent that made it impossible for Manager Corp. to act.

f. Chambers argued that the court's actions ran counter to the terms of the Metcalf Associates operating agreement that required unanimous consent to sell. The court of appeals responds to this argument stating:

"[T]his was not a situation in which members had a mere disagreement regarding the specific sales price of a company asset to
a third party [in which case they could properly refuse to consent, avoid the required unanimity under the operating agreement, and avoid a sale]. The evidence showed a fundamental disagreement between Hayes, who wanted to sell all of the buildings within a short time, and Chambers, who ultimately wanted to acquire the fifth building for himself as a long-term investment.”

1. The trial court found that the business purpose of Metcalf Associates was to buy and sell buildings – with a relative short turn-around.

2. The fundamental disagreement was over whether this business purpose would be pursued as to the fifth building.

g. More importantly, the trial court found that the situation was such as to potentially cause irreparable injury to Metcalf Associates.

1. This finding can be made even though the business may be currently operating at a profit.

2. The statute includes “suffering . . . irreparable injury” or “threatened” irreparable injury. The court need not wait until there is actual injury to act to avoid injury.

B. Banking Transactions


a. National Bank of Andover (“Bank”) obtained a Financial Institution Crime Bond from Kansas Bankers Surety Company (“KBS”). The Bank completed an application in which it responded to three questions relating to practices and procedures the Bank followed to detect employee wrongdoing. The application, which became part of the insurance contract, stated:

“THE INSURED REPRESENTS THAT THE INFORMATION FURNISHED IN THIS APPLICATION IS COMPLETE, TRUE AND CORRECT. ANY MISREPRESENTATION, OMISSION, CONCEALMENT OR ANY INCORRECT STATEMENT OF A MATERIAL FACT, IN THIS APPLICATION OR OTHERWISE,
SHALL BE GROUNDS FOR THE RESCISSION OF ANY BOND
ISSUED OR RENEWED IN RELIANCE UPON SUCH
INFORMATION.”

b. After the bond had been renewed, the Bank discovered that one of its employees had been making false entries in the Bank’s records to conceal payment of insufficient funds checks for three customers. This had taken place over a three-year period and amounted to a loss of almost $900,000.

c. When the Bank sought payment under the KBS bond, KBS conducted an investigation and found the Bank had failed to correctly answer one or more of the questions relating to the Bank’s practices and procedures. KBS therefore sought to rescind the bond and refused payment of the Bank’s claims.

d. Issue at trial court and court of appeals: whether a bond provision, allowing for rescission for something less than fraudulent misrepresentation, was illegal or otherwise against public policy. The Kansas Supreme Court concludes that under Kansas law:

“[I]nsurer KBS may rescind a policy which expressly allows rescission for conduct less serious than fraudulent misrepresentation by its insured bank. Such a contract between these two sophisticated commercial entities does not contravene public policy and is not illegal. It should be enforced as written. . . . [T]he trial court erred in failing to honor the agreement between the parties and to instruct the jury consistent with the contract. The error is reversible.”

e. Court holds the questions contemplated something more than a mere statement that the Bank had adopted established policies and procedures. Instead, the questions required that the Bank had been, and was currently, implementing the policies and procedures.


a. Santa Rosa KM Associates, Ltd. sought to prepay a commercial loan it renegotiated and assumed in 1998. The original amount borrowed in 1991 was $6,375,000; the loan balance when Santa Rosa sought to prepay the loan in 2005 was $4,865,142. The note was otherwise due
in 2017.

b. The promissory note to Principal Life Insurance Company entitled Principal to a “make whole premium” in the event Santa Rosa sought to prepay the loan.

(1) Under the “make whole premium” formula Santa Rosa was obligated to pay $1,636,268 to Principal in order to prepay the $4,865,142 loan balance.

(2) Santa Rosa commenced a declaratory judgment action seeking to have the “make whole premium” declared unenforceable.

c. Trial court upheld the prepayment fee but denied Principal’s request for attorney fees relying upon a pre-amendment version of K.S.A. § 58-2313 and the terms of the attorney fees provisions found in the note and mortgage.

d. The court of appeals upholds the trial court’s ruling on the prepayment fee but reverses on the attorney fees issue.

e. The court characterizes the issue, and the claims made by Santa Rosa, as simply whether the prepayment fee violates Kansas public policy.

(1) Although noting the fee at issue in this case is not liquidated damages, because there has been no failure to perform by Santa Rosa, the court looks to liquidated damages principles to evaluate the reasonableness of the prepayment clause.

(2) The court evaluates the reasonableness of the prepayment clause considering the knowledge and concerns of the parties at the time they entered into the transaction.

(3) Noting the goal is to avoid a “heads I win, tails you lose” proposition against the lender when the borrower can freely prepay the loan whenever interest rates drop in the future, the court observed:

“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.”

f. The court also rejects Santa Rosa’s unconscionability claim.

(1) The court found, as a matter of law, there was nothing about the prepayment clause to suggest it was substantively or procedurally unfair.

(2) The clause was clearly presented in a transaction between sophisticated parties; the amount of the prepayment fee was simply “a function of the amount of the unpaid balance on the loan and the disparity in prevailing interest rates between the time the loan originated and the time of it proposed prepayment.”

(3) The court also notes: “The time for prepayment was in Santa Rosa’s exclusive control.”

g. The court reverses the trial court on the attorney fees issue.

(1) Trial court denied Principal’s request for attorney fees noting first that when the original parties entered into the note and mortgage in 1991, K.S.A. § 58-2312 prohibited the collection of attorney fees from a consumer in a consumer credit transaction.

(2) However, in 1994 § 58-2312 was amended, along with a similar prohibition in the UCCC, to permit attorney fees provisions in any note, mortgage, or other credit agreement. K.S.A. § 58-2312 has provided, since 1994:

58-2312. Stipulation for attorney fees void. 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.

(a) The trial court held the 1994 amendment did not apply since the original note and mortgage were entered into
in 1991.

(b) The court of appeals holds that a new note and mortgage were entered into in 1998 when Santa Rosa and Principal renegotiated the loan as a condition to Principal approving assignment of the property and debt obligations by the original borrower to Santa Rosa.

(3) The court also rejects the trial court's interpretation of the attorney fees provisions in the note and mortgage as applying only to collection efforts in the event of default. A declaratory judgment defining contractual rights under the note and mortgage is an action to enforce rights under the note and therefore an action "in any way affecting or pertaining to this mortgage, the Note or the premises" as contemplated by the attorney fees provision in the mortgage.

3. **Mortgagee has no duty to a purchaser at a foreclosure sale to ensure that all lien holders have been properly joined in the foreclosure action.** *First National Bank and Trust Co. v. Wetzel*, 42 Kan. App.2d 924, 219 P.3d 819 (2009).

a. First National Bank and Trust Co. in Larned ("FNB") filed a mortgage foreclosure action against its mortgagor. Some of the property was sold at the foreclosure sale by the sheriff to Wetzel for $200,000.

b. When it was discovered, through the public records, there were other creditors with liens against the property that were not named in the foreclosure action, the judgment debtor was able to have the sale set aside and the purchase money returned to the successful bidders.

c. Wetzel intervened in the action and sought to have FNB compensate it for interest it paid to another bank on a loan to purchase the property. The trial court, purporting to apply equitable principles, held FNB was obligated to pay Wetzel $3,709.42 in damages representing interest Wetzel paid on the loan for the aborted sale.

d. Court of appeals reverses the trial court holding FNB owed no duty to Wetzel regarding the condition of title to property sold at the foreclosure sale.
The court reasoned that since a foreclosure sale is a judicial sale, the purchaser receives the equivalent of a quitclaim conveyance of the property with the duty to search the chain of title to determine what the seller had to convey.

The duty is on the purchaser, not the seller, to ascertain the status of title to the property; a purchaser's failure to investigate title to the property is negligence and equity will not allow them to recover for their own negligence.

C. Commercial Law Issues

1. Court holds plaintiffs under the Kansas Consumer Protection Act asserting "willful" conduct must prove the defendant had "an intent to harm the consumer." *Unruh v. Purina Mills, LLC*, 289 Kan. 1185, 221 P.3d 1130 (2009).

   a. Farmers Unruh and Carter purchased a cattle feeding supplement system sold by Purina. The system did not work as represented and Unruh and Carter sued Purina for breach of warranty and violation of the Kansas Consumer Protection Act (KCPA).

   b. The jury found in favor of Unruh and Carter and awarded damages. The trial judge awarded attorney fees to Unruh and Carter under the KCPA.

   c. Court of Appeals reversed as to the KCPA claim holding plaintiffs failed to establish Purina’s violation of the KCPA was "willful."

   d. Kansas Supreme Court agreed with the Court of Appeals that "willful" action under the KCPA requires an "intent to harm the consumer."

   However, the court held the jury had sufficient evidence to support a finding that Purina’s actions were willful under the "intent to harm" standard.

Reversing the Court of Appeals on its application of the willful standard, the court held that since the KCPA was violated Unruh and Carter were entitled to attorney fees as the prevailing party.
e. Justice Rosen, joined by Justices Davis and Biles, makes a convincing argument in his dissenting opinion that the “willful” standard adopted by the majority is not consistent with the Legislature’s intent.

(1) The majority gives substantial weight to the origin of a jury instruction on what is “willful” conduct.

(2) The dissent noted that a jury instruction has little relevance when seeking the intent of the Legislature under a modern consumer protection law expressly designed “to protect consumers from suppliers who commit deceptive and unconscionable acts.”

f. Consumers will now be burdened with establishing not only that a deceptive act has been committed, but also that the supplier intended to harm the consumer through the deceptive act.


a. Contract interpretation under Article 2 of the Uniform Commercial Code (UCC) follows a distinct statutory process where, like its common law counterpart, the task is to first identify the terms of the contract followed by an analysis of what the terms mean.

b. Ascertaining the terms of the contract is governed by the parol evidence rule. The Article 2 version of the parol evidence rule is found at K.S.A. 84-2-202.

c. The original contract between the parties required Foundry to manufacture custom light fixtures that would be delivered to Cravotta by a specified date. Although not expressly stated in the parties’ agreement, it appeared Cravotta would have to be actively involved in the process to provide engineering and aesthetic input to ensure the fixtures were safe and achieved the look desired by Cravotta’s client.

d. When Foundry was unable to comply with delivery obligations created by the express terms of the contract, Cravotta sued resulting in a settlement agreement which is the focus of this litigation. When Foundry failed to deliver the goods as specified in the settlement agreement, Cravotta sought enforcement of the settlement agreement.
e. Issue: Whether Foundry was relieved of its failure to perform because Cravotta failed to provide the necessary engineering and aesthetic input Foundry required to manufacture the final product.

(1) Foundry argued its performance was subject to a condition precedent that Cravotta provide the input necessary to enable Foundry to perform.

(2) To establish this understanding, which was not expressly stated in the settlement agreement, Foundry sought to introduce extrinsic evidence that would supplement the terms of their agreement.

(3) The trial court held that to consider such extrinsic evidence would violate the “statute of frauds” because the provisions were not contained within the parties’ writing that constituted their agreement.

f. Trial court reversed by court of appeals: The Court of Appeals reverses and remands finding the trial court employed the wrong analysis to determine whether the parties’ agreement included the obligation for Cravotta to provide input as a condition to Foundry’s duty to perform.

g. The trial court improperly focused on the statute of frauds when it should have been focusing on the parol evidence rule.

(1) It was clear that the parties’ agreement complied with K.S.A. 84-2-201, the Article 2 version of the statute of frauds.

(2) There was a writing to support the agreement and K.S.A. 84-2-201(1) provides: “A writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing.”

h. The real issue: whether the omitted term could be fairly implied from the express terms contained within the writing.

(1) This, in the first instance, is a parol evidence rule issue. To determine the extent to which evidence of terms not expressly referenced in the writing can be considered part of the contract, the first step is to determine whether the contract is
"integrated."

(2) The Article 2 parol evidence rule is found at K.S.A. 84-2-202 which provides:

"Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented

(a) by course of performance, course of dealing or usage of trade K.S.A. 2009 Supp. 84-1-303, and amendments thereto); and

(b) by evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement." (Emphasis added).

i. Under the UCC, even an “integrated” agreement can be “explained or supplemented” by course of performance, course of dealing or usage of trade.

(1) The integrated agreement can also include “consistent additional terms.”

(2) If the agreement is found not to be “intended by the parties as a final expression of their agreement,” there is no restriction on the use of extrinsic evidence.

(3) If the agreement is “integrated” the next inquiry is whether it is a “complete and exclusive” integration which would exclude evidence of consistent additional terms. It would not, however, prevent the fully integrated agreement from being explained or supplemented by course of performance, course of dealing or usage of trade.
j. The court notes that questions regarding integration, the degree of integration, and the existence of a course of performance are all factual issues that must be addressed at the trial court level before the parties' obligations can be determined. Therefore, the court remands the case to the trial court to ascertain the precise terms of their agreement. Once the terms are identified, the court should be able to interpret the terms to ascertain the intent of the parties regarding any conditions precedent Cravotta must satisfy before Foundry is obligated to perform.


1. Interpleader action filed by the Shamberg, Johnson & Bergman firm for court direction on who was entitled to $582,881.90 referral fee.

2. Michael P. Oliver was a member of the Wallace, Saunders, Austin, Brown & Enochs, Chartered law firm when he was contacted by the family of Sara Hotchkiss to assist them with her serious medical problems which eventually became the focus of a potential medical malpractice claim.

3. Because Wallace, Saunders engaged in primarily medical malpractice defense work, it had a policy against suing medical care providers. Therefore, Oliver proposed referring the case to another firm and accompanied the Hotchkiss family to meet with two attorneys. Ultimately, they selected Victor Bergman of the Shamberg firm to represent them.

4. On January 8, 2003 Sara Hotchkiss and her husband entered into an employment agreement with the Shamberg firm in which they agreed to a contingent fee of 40% of the net recovery after expenses.

5. The parties ultimately agreed to the following fee sharing arrangement:

10% of the first $100,000 of net attorney fee; plus
15% of any net attorney fee from $100,001 - $250,000; plus
20% of any net attorney fee from $250,001 - $500,000; plus
25% of all net attorney fee greater than $500,001.
"The letter said that Shamberg would be responsible to advance all of the expenses of litigation and do all of the work. It also stated that if the Hotchkisses needed assistance with obtaining governmental benefits, Wallace Saunders would either help them or assist them with an appropriate referral. Bergman also requested Oliver to accompany him for an off-the-record visit with a physician."

7. This lawsuit arose when Oliver left the firm effective January 31, 2005. The Hotchkiss family asked that Oliver continue acting as their attorney. Some of the physicians settled with Hotchkiss on July 11, 2005; the other defendants settled during trial with the settlement being approved on September 2, 2005. These settlements resulted in the $582,881.90 referral fee which was claimed exclusively by Oliver and by the Wallace, Saunders firm. Shamberg filed the interpleader action on September 16, 2005.

8. For a discussion of the Hotchkiss trial, and how the $6.5 million settlement arose, see the discussion in the Shamberg firm’s Winter 2005 Newsletter which can be accessed on-line at: http://www.sjblaw.com/CM/Newsletters/2005-winter.pdf

9. The trial court held the referral fee belonged to the Wallace, Saunders firm; the supreme court held that under the firms’s Deferred Compensation Agreement had the Hotchkiss family elected to keep the case with Wallace, Saunders, Oliver would be entitled to payment of $5.22 as full compensation for his interest in the case. However, since the Hotchkiss family requested that Oliver continue to represent them, under the Deferred Compensation Agreement the Wallace, Saunders firm was fully compensated for its interest in the case when Oliver paid them $150. Therefore, Oliver, as the owner of the file, was solely entitled to the $582,881.90 referral fee.

10. Observations regarding referral fees by the Kansas Supreme Court in the Shamberg case:

   a. The supreme court characterizes the trial court’s view of the referral agreement as follows:

   “Apparently, the district court viewed the referral agreement as a stand-alone contract for the sale of the medical malpractice claim and determined that Wallace Saunders had completed its performance and
earned it referral fee when the client was delivered to Shamberg. We cannot accept that characterization. ‘A client is not an article of property in which a lawyer can claim a proprietary interest, which he can sell to other lawyers expecting to be compensated for the loss of a property right.’”

b. Instead, the supreme court states: “The referral agreement must be viewed in the context of the duties which are owed to the client.”

c. At the time Wallace Saunders entered into the referral agreement, it had committed to representing Hotchkiss, through its agent Oliver.

(1) Wallace, Saunders argued its duties to Hotchkiss ended when it turned her over to competent trial counsel to handle her case.

(2) This timing issue was important because Wallace, Saunders was later handling matters for the hospital that was being sued by Hotchkiss.

(3) The court refused to consider this conflict issue noting this was a contract dispute between Oliver and his former law firm. It is not a suit by Hotchkiss seeking any sort of redress against Wallace, Saunders.

(4) The court notes that if Oliver believed Wallace, Saunders violated the Kansas Rules of Professional Conduct, Oliver had a duty to report the matter to the Disciplinary Administrator pursuant to RULE 8.3(a): “A lawyer having knowledge of any action, inaction, or conduct which in his or her opinion constitutes misconduct of an attorney under these rules shall inform the appropriate professional authority.”

(5) Neither the supreme court, or the trial court, exhibited any willingness to consider ethical arguments to bolster Oliver’s contract claims against the law firm. The court recites the following from the “SCOPE” introductory material to the Kansas Rules of Professional Conduct (now found at ¶ [20]):
“Violation of a Rule should not itself give rise to a cause of action against a lawyer nor should it create any presumption in such a case that a legal duty has been breached. In addition, violation of a Rule does not necessarily warrant any other nondisciplinary remedy, such as disqualification of a lawyer in pending litigation. The Rules are designed to provide guidance to lawyers and to provide a structure for regulating conduct through disciplinary agencies. They are not designed to be a basis for civil liability. Furthermore, the purpose of the rules can be subverted when they are involved by opposing parties as procedural weapons.”

11. Basic guiding principles for referral fees in Kansas:

a. Whatever fee is made with the client must be “reasonable.”

b. Assuming the contingent fee arrangement is reasonable, the attorney entitled to the fee can enter into an agreement with a referring attorney to share part of the fee.

c. The most important aspect of the “reasonableness” of the fee-sharing arrangement is that it will not in any way result in an increased fee to the client.

(1) The fee charged the client would be the same even if there was not a fee sharing arrangement with a referring attorney.

(2) This was a point stressed by the court in the Shamberg case.

d. The second requirement is that the “client is advised” that a referral fee will be paid to the referring attorney – and the client “does not object to the division.”

e. The referring attorney need not take any active involvement in the referred case. However, the referring attorney could be responsible for a referral to an attorney not equipped to competently handle the matter.
f. See Ryder v. Farmland Mutual Ins. Co., 248 Kan. 352, 807 P.2d 109 (1991); Think Ethics, Getting Paid for Doing It Right! 64 J. KAN. BAR ASS’N 4 (Oct. 1995) (“Hopefully, lawyers put the rule to good use these days, not only to get paid for referring a fee, but to make it worthwhile to refer the case properly. Referring the case properly insures the client gets the best possible advice.”).

12. Rationale for Kansas’ liberal policy promoting referral fees: The client is benefitted because the referring attorney has the incentive to find them the best counsel possible to address their problem – and the ultimate fee to the client will be the same.

II. CONTRACT LAW

A. Useful Contract Clauses


a. One of the odder foundations of contract law is that the lawyer can provide for compensation in the event the other party breaches the contract, but it is improper to include provisions specifically designed to coerce the other party to perform their contractual obligations.

(1) This is commonly expressed as the line between legal compensatory liquidated damages and illegal coercive penalties. Note this also supports the concept of “efficient breach.”

(2) Liquidated damages assist the parties in determining whether it is more economic to breach a contract as opposed to perform the contract.

b. During our 2008 Recent Developments program, and again in 2009, 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.

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).

h. The materials that follow illustrate how students in my Advanced Oil and Gas Law class, when asked to draft a liquidated damages clause for their client, used the Kansas Supreme Court's teachings in Carrothers to create defensible, informed, and effective contract language.
ADVANCED OIL & GAS LAW
EXERCISE #13

INTRODUCTION TO DRAFTING
LIQUIDATED DAMAGES CLAUSE
FARMOUT AGREEMENT

Due Date & Time: Tuesday, April 6, 2010 at 9:00 a.m.
   Turn In to Shirley Jacobson, Room 302

Goal of Exercise: To learn how to prepare a liquidated damages clause.

Resources: Use the information provided to you in conjunction with Exercise #9, use the form of Farmout Agreement you have been given, and conduct whatever additional research you deem necessary to accomplish the assigned task.

Procedure: Obtain an exam number for this exercise from Shirley Jacobson in Room 302. Draft a clause to address the issues identified in the Facts that follow. The clause will be used to replace paragraph 2.E. of the form Farmout Agreement you have been given.

Facts

Dock Hillard owns the following oil and gas leases:

Lessors: Will Pierce  
Lease Date: May 15, 2007  
Primary Term: 3 Years  
Bonus Paid: $5,000  
Delay Rental: $1,000  
Description: North Half of Section 2, Township 27 South, Range 15 East of the 6th Principal Meridian in Wilson County, Kansas.
Lessors: Cody Pierce
Lease Date: May 15, 2007
Primary Term: 3 Years
Bonus Paid: $5,000
Delay Rental: $1,000
Description: South Half of Section 2, Township 27 South, Range 15 East of the 6th Principal Meridian in Wilson County, Kansas.

You can assume that the other terms of these leases are identical to the form we have been working with in the course (as well as in the basic Oil and Gas Law course). These leases will be listed as the farmout acreage on Exhibit A to the Farmout Agreement.

Dock is negotiating a Farmout Agreement with Acme Oil Company. The parties have agreed to work with the attached document. They have agreed to all the terms but are currently negotiating a liquidated damages clause to replace paragraph “2.E. Failure to drill.” As the clause reads now, the only effect of Acme failing to drill the test well described in section 2 is that the agreement will terminate and Acme will not have an opportunity to earn leased acreage under the Farmout Agreement.

This is not acceptable to Dock because his primary reason for farming out to Acme is to ensure a well is drilled that will, if productive, hold the farmout acreage by production. Therefore, Dock wants to do whatever he can to ensure Acme drills the well; but if he doesn’t, Dock wants to ensure he is fully compensated for the maximum amount possible. There has been successful drilling in the area around this leased land, resulting in substantial gas discoveries; Dock believes his leases are at an optimal location. However, Dock at this time does not have the funds to drill on this acreage so he is motivated to farm out to Acme if he can obtain the terms he desires.

[NOTE: The students were given a copy of a Farmout Agreement.]
Memorandum of Law

To: Dock Hillard  
From: Exam #001  
Date: 2 March 2010  
Subject: Drafting a Liquidated Damages Clause

The liquidated damages clause is used to contractually agree in advance on what a party’s damages will be in the event the other party fails to perform. Carrothers Constr. Co. v. City of S. Hutchinson, 207 P.3d 231, 241 (Kan. 2009). Drafting the clause requires special care because it is against public policy to compel a party to perform their contractual obligations by imposing a financial “penalty” for non-performance. Id. Assessing an amount in excess of a party’s anticipated loss would be an improper award of punitive damages for a breach of contract. Restatement (Second) of Contracts § 356(1), cmt. a (1981). Therefore, the goal is to ensure the liquidated damage clause is designed to merely compensate the non-breaching party for the anticipated loss they will suffer from the other party’s non-performance. Carrothers, 207 P.3d at 241.

To have an enforceable clause, the Kansas Supreme Court requires that at the time the parties enter into their contract: (1) damages are difficult to calculate in the event of a breach; and (2) the liquidated damage figure used is a reasonable estimate of what the damages might be in the event of a breach. Id. In Kansas these issues are examined solely upon the facts and circumstances as of the time the parties enter into the contract; the court will not engage in any sort of comparison of the liquidated damage number with the actual damage number to evaluate the reasonableness of the liquidated number. Id.

Actions that can be taken to support the effectiveness of a liquidated damages clause include: (1) identifying in the document why it is difficult to determine, with accuracy, damages in the event of a breach; and (2) engaging in an analysis, at the time of contracting, of damages that might be incurred in the event of various failures to perform. This information can then be used to arrive at appropriate liquidated damages for stated events of non-performance and also alerts the other contracting party, and a reviewing court, to any consequential damages that might not be readily apparent. The clause should include a recitation of the potential damages and the efforts to ascertain likely damage ranges prior to selecting the ultimate liquidated damages figure. In upholding the liquidated damages clause in Carrothers the court was impressed with how the parties focused on the risk of a delay in performance, the difficulty in ascertaining damages while nevertheless engaging in an informed projection of probable loss resulting from a delay, and the parties’ clear intent to use liquidated damages to address delay. Id. at 242, 243.

Structural drafting guides include ensuring the provision is “plainly identified” in the contract by labeling the clause with an appropriate heading, such as “Liquidated Damages.” Id. at 236 (court notes the clause was “plainly identified”). Avoid any language that suggests coercion or penalty. Instead, speak in terms of compensating the non-breaching party for their losses. Focus on a desire to protect the contracting parties from the difficulty, uncertainty, and expenses associated with trying to ascertain actual damages in a judicial proceeding. Id. at 241.
E. **Failure to drill; farmee must pay liquidated damages.** If farmee fails to drill the test well required by § 2, or otherwise fails to take action to maintain the leases as necessary to drill the test well and determine whether to complete it as a producer, farmee will be obligated to compensate farmor by paying farmor $875,000 in liquidated damages. Farmor and farmee acknowledge that:

1. Failure to comply with § 2 of this agreement would result in the leases terminating and an inability to confirm whether the leased lands contain valuable hydrocarbons;

2. The amount of damage resulting from farmee’s failure would not be easily and readily determinable;

3. They desire to protect themselves against the difficulty, uncertainty, and expenses associated with trying to ascertain actual damages; and therefore

4. They desire to stipulate, by agreement, what they mutually believe is a reasonable estimate of probable damages and in an amount they believe is conscionable considering the value of the subject matter of this agreement and the probable loss in the event farmee fails to perform.

In arriving at the amount of liquidated damages the parties have considered the following facts and circumstances: There has been successful drilling in the area around the leases, resulting in substantial gas discoveries, and the leases appear to be at an optimal location in relation to the discoveries. Although farmor has invested $14,000 in acquiring and maintaining the leases, their current market value exceeds $200,000. The only way to test the leases for the presence of oil or gas is to drill a well. Discoveries in the area have been made at depths ranging from 3,500 to 3,750 feet below the surface. To adequately test the leases a prudent operator would drill to a depth of 4,000 feet which would typically be done under a standard footage drilling contract for the area at a cost of approximately $475,000.

Farmee’s failure to drill will therefore likely result in farmor: Losing its leases valued at $200,000; losing the value of having the promised well drilled at a cost of $475,000; plus the potential loss of substantial profits in the event the gas reservoir trends under the leases as the parties predict. These lost profits are most difficult to predict but would certainly exceed $200,000 based upon the production rates and operating costs associated with surrounding wells.

a. In 1998 Ritchie Corp. sold 16.8 acres to BFI Waste Systems of North America, Inc. (BFI) [Waste Connections is the successor to BFI]. The acreage consisted of a landfill and a waste transfer station. As part of the sale Ritchie retained a reversionary interest in the transfer station acreage which required BFI to pay a sum per ton of waste processed at the transfer station. At the end of 35 years Ritchie would receive the transfer station acreage back pursuant to its reversionary interest.

b. The agreement contained the following clause concerning the transfer station:

   **"Right of First Refusal."** At all times this escrow agreement is in effect Buyer shall have a right of first refusal with respect to Seller’s interest in this escrow agreement, including without limitation Seller’s reversionary interest in the Property, however designated, to the effect that upon receipt by Seller of any offer to purchase Seller’s interest in this Agreement or the Property by a third party, Seller shall give written notice to Buyer of the fact and terms of such third party offer. Buyer shall have forty-five (45) days after its receipt of such notice to notify Seller in writing of its election to purchase such interest(s) on such financial terms (the “Election Term”). In the event Buyer does not notify Seller of its election to purchase such interest(s), then Seller may sell such interest(s) on such identical terms to such third party so long as such sale is consummated within ninety (90) days after such Election Term. If such sale to the third party is not consummated within such period, then the Buyer shall again have the right of first refusal to purchase such interest(s) prior to any sale to any third party. This right of first refusal shall specifically not apply to any transfer or assignment by Seller to an affiliate of Seller or to any stockholder of Seller or any of their affiliates.”

c. A detour to address a **RULE 1.1 Competence** consideration.
"A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation."

d. As an aside, since the escrow agreement was for 35 years, under the Kansas common law rule against perpetuities it could be argued the entire clause would be void.

e. Kansas has traditionally applied the rule against perpetuities to preferential rights to purchase. See generally Gore v. Beren, 254 Kan. 418, 867 P.2d 330 (1994) (rule not violated because interest would vest within a life in being at the time of its creation—otherwise the court noted: “Agreements creating an option or preemptive right to purchase real estate constitute property interests which are subject to the rule against perpetuities.”).

f. Ritchie could elect to sell the transfer station at any time during the 35-year escrow term. This sale would trigger, at that time, the springing executory interest in BFI to acquire the interest which would be viewed as a non-vested future interest in the transfer station held by Ritchie.

g. Because it is not possible to state that the event triggering BFI’s future interest (sale by Ritchie) in the land will, or will not, occur (vest) within 21 years from the date of sale, December 29, 1998 (it could be up to 35 years after), the interest, at common law, would be void.

h. However, Kansas, effective July 1, 1992, adopted the Uniform Statutory Rule Against Perpetuities, K.S.A. §§ 59-3401 to 59-3404 (2005). This statute can save the preferential right from the rule in this case in two ways:

(1) Under the “wait-and-see” provision which provides the interest is valid if it “either vests or terminates within 90 years after its creation.” K.S.A. § 59-3401(a)(2) (2005). In this case, Ritchie will either sell, or not sell, the interest within 35 years so we know it will either vest or terminate in 90 years.
(2) Under the facts this commercial transaction is a “nondonative transfer” which is no longer subject to any rule against perpetuities restrictions pursuant to K.S.A. § 59-3404(1). Therefore, we would not have to resort to any of the savings provisions of the Act (such as the 90-year wait-and-see provision) because the transaction is taken completely out of the rule’s operation.

i. We have a potential problem in Kansas – caused primarily by me. I believe the Uniform Statutory Rule Against Perpetuities is void in Kansas because it was enacted in violation of Article 2, Section 16 of the Kansas Constitution which states:

“No bill shall contain more than one subject, except appropriation bills and bills for revision or codification of statutes. . . .”

(1) The original bill which contained the Uniform Statutory Rule Against Perpetuities also contained two other provisions: repeal of the Bulk Sales Act and statutes adopting a conservation easement program. All three concerned some version of a “uniform law” as adopted by the National Conference of Commissioners of Uniform State Laws (Uniform Law Commission).

(2) This precise issue was addressed in Larson Operating Co. v. Petroleum, Inc., 32 Kan. App. 2d 460, 84 P.3d 626 (2004). The log-rolling history of the bill was not presented; the court of appeals’ decision is unconvincing. Review by the Kansas Supreme Court was not sought. Basic position of the court:

“Here the subject matter of the enactment did not embrace ‘dissimilar or discordant subjects’ but rather embraced a singular purpose: amendment and enactment of certain uniform acts in an attempt to harmonize them with Kansas legislative intent. [what?] Joinder of these enactments and amendments of uniform laws in a singular enactment did not offend the constitution, since there was no obvious intent to tie a matter of legislative merit to an unworthy matter.”
The court's analysis amounts to: if you put the word "uniform" in the title of the act, then they all have one thing in common, they are "uniform" acts. So, the "uniform" death penalty act could be considered in conjunction with the "uniform" partial birth abortion act?


(1) Holland & Hart represented Buell Development Corporation in connection with the sale of stock in Kings County Development Corporation to John Rocovich. The issue concerned an option in favor of Buell to acquire from Rocovich a percentage of the Development Corporation's minerals in California in the event Development Corporation ever decided to distribute these interests to its shareholders.

(2) Rocovich apparently had some level of control over Development Corporation where he could initiate the corporate action to cause the distribution of minerals to its shareholders.

(3) Dispute arose over whether this option violated the rule against perpetuities (among other claims), and Buell settled the matter by reducing its right to share in a distribution of minerals. The jury valued this reduction at $3,364,011, plus $2,125,195 in interest. Trial court: found the agreement violated the rule against perpetuities and the law firm was negligent for not addressing the matter properly.

(4) On appeal the court reverses noting that it was not possible for Buell and Rocovich to in any way contract to create a perpetuity as to property owned by a third party, Development Corporation. Therefore, the agreement did not violate the rule against perpetuities.

(5) But wait, we are not done with you. We are remanding the
case so Buell’s malpractice claim can be considered in light of the fact the agreement did not violate the rule against perpetuities. Instead, the issue is whether the attorneys were negligent by not recognizing “the clear potential for dispute” associated with the rule against perpetuities, and then failing to take the necessary action by drafting the agreement to avoid a potential perpetuities claim.

k. Once we get past the rule against perpetuities, we come to the major problem with the preferential right to purchase: the package transaction.

(1) Lots of litigation where a party has a preferential right to purchase property “A” which is subsequently sold in a transaction consisting of properties “A” and “B” and the selling/buying party tries to avoid an exercise of the preferential right by loading up the purchase price on the “A” part of the transaction.

(2) Package transactions have many other problems. For example, can the preferential rights holder insist that: (1) it can buy the entire package for the package price? (2) property “A” can only be sold separately? Can the preferential rights holder be forced to bid on the entire package or none at all? If they are not required, or able, to purchase the package – how will the package purchase price be allocated to the single preferential rights property? See generally Navasota Resources, L.P. v. First Source Texas, Inc., 249 S.W.3d 526 (Tex. Ct. App. 2008).

l. Risks for everyone:

(1) The attorney representing the seller of the property burdened by the preferential right. To what extent can the attorney assist their client in avoiding the limitations of the preferential right by making literal use of the terms of the contract?

(a) For example, the clause involved in the Waste
Connections case states: “This right of first refusal shall specifically not apply to any transfer or assignment by Seller to an affiliate of Seller or to any stockholder of Seller or any of their affiliates.”

(b) Could the seller’s attorney suggest that the asset burdened by the preferential right be transferred to “an affiliate of Seller” and then have the stock (not the asset) in the affiliate sold to the desired buyer?

(c) Rule 8.4 Misconduct. “It is professional misconduct for a lawyer to: ... (c) engage in conduct involving dishonesty, fraud, deceit or misrepresentation . . . .”

(d) What if the conduct is approved by the Texas Supreme Court? Tenneco Inc. v. Enterprise Products Co., 925 S.W.2d 640 (Tex. 1996). Court holds that a transfer of stock is not a transfer of the company’s assets and therefore, unless the preferential rights provision states otherwise, a stock transfer is not a triggering event. This has given rise to the “Texas Two-Step” approach for avoiding preferential rights provisions.

(i) Do you then have a duty to counsel your client on this available option?

(ii) To what extent will Texas law on this issue transfer to other jurisdictions? Kansas?

(iii) Practical considerations: litigation magnet.

(2) The attorney representing the seller of the property burdened by the preferential right. To what extent can the attorney assist their client in avoiding the limitations of the preferential right by manipulating the purchase price allocation?
(a) **Rule 8.4 Misconduct.** "It is professional misconduct for a lawyer to: . . . (c) engage in conduct involving dishonesty, fraud, deceit or misrepresentation . . . ."

(b) In *Waste Connections* the dispute was over purchase price allocation. The total purchase price was $4.95 million, the seller allocated $2 million to the transfer station, but the buyer, in the event BFI/Waste Connections exercised its option, would still be obligated to pay $3.5 million for the landfill portion of the package.

(c) No deceit here because all the relevant facts were clearly stated in the sales agreement between Ritchie (seller) and Cornejo (buyer). Their agreement stated:

"2.1 Purchase Price and Payment. The purchase price for the entirety of the Assets [landfill and transfer station] shall be Four Million Nine Hundred Fifty Thousand Dollars ($4,950,000), payable in cash or certified funds at Closing, of which Two Million Dollars ($2,000,000) will be allocated to and paid to Ritchie Corporation for the purchase of its rights and the assumption of its obligations under the Escrow Agreement."

"In the event that Waste Connections of Kansas, Inc. shall, upon receipt and due and proper notice from Sellers, elect to exercise its right of first refusal under the Escrow Agreement, the parties agree that the purchase price for the remaining Assets shall be Three Million Five Hundred Thousand Dollars ($3,500,000.00), payable in cash or certified funds at Closing."

(d) Notice of the sale was provided to Waste Connections, along with a copy of the Cornejo/Ritchie agreement. Ritchie indicated in the notice that it had "received an offer to acquire its interest in the escrow agreement for $2,000,000.00 cash as specified in the
attached Asset Purchase Agreement. . . .”

(e) Waste Connections tendered $2 million but also sought to preserve its rights to argue the purchase price should be $1.45 million ($4.95 million - $3.5 million).

(f) Waste Connections sued Ritchie, trial court held for Ritchie and awarded Ritchie $108,972.15 in attorneys fees pursuant to the prevailing party attorney fees provision in their agreement. The court of appeals reverses finding that allowing Ritchie to obtain $2 million for what Cornejo was willing to pay only $1.45 million “would evade the ‘spirit of the bargain . . .’”

(g) The court concludes: “Ritchie acted in bad faith by attempting to maximize its profits to ‘recapture opportunities foregone’ through granting of the right of first refusal.”

(3) The attorney representing the buyer of property subject to the preferential right to purchase. The buyer cannot merely accommodate whatever scheme the seller may come up with to negate another party’s preferential right to purchase.

(a) Tortious interference issues.

(b) The attorney advising the buyer must be as attuned to the situation as the attorney advising the seller.

(c) The buyer may become the enabler.

m. Observations by the *Waste Connections* court regarding the “package deal”: 
“The package deal is a risky situation in the terms of the right of first refusal. There is ‘a risk in package deals that the purchase price may be unfairly allocated or padded to defeat the rights of first refusal.’ . . . . In a package deal situation, more protection needs to be given to the right of first refusal to prevent collusion or bad faith. In a package deal, the purchase price should come under greater scrutiny and any doubt in the amount should be resolved to protect the right of first refusal.”

“In the context of a package deal involving a right of first refusal, the price for the total package generally should not fluctuate based upon whether the right of first refusal is executed. Ritchie should not be able to receive more money after exercise of the right of first refusal. For the right of first refusal to be given its lawful effect, Ritchie should be in the same financial position regardless of whether WCK exercises the first refusal.”

“Because there are a multitude of ways that a sale can circumvent a grantee’s right of first refusal in a package deal, the duty of good faith and fair dealing should be applied prominently in cases like the one before us.”

n. The drafting response would be to address the problem head-on in the next document, having learned the most recent lessons of avoidance and abuse.


a. Consistent with the strong freedom of contract positions taken by the Kansas Supreme Court in recent years, the Court of Appeals enforces two contract clauses that significantly restrict a home buyer’s remedies.

(1) The first clause was contained in a house inspection contract
between Sheila Santana and Tom F. Beard Inspections, LLC ("TFB").

(2) Santana hired TFB to inspect a house she was purchasing from Mary Olguin.

(3) After purchasing the house Santana discovered “animal odors and damage, dry rot in wood trim elements, and evidence of past water leakage.” When she sued TFB for negligence, fraud, and violations of the Kansas Consumer Protection Act (KCPA), TFB was granted summary judgment because of a release and limitation of liability contained in the inspection contract between Santana and TFB.

(4) In the contract Santana “releases and exempts . . . [TFB] from all liability and responsibility for the cost of repairing or replacing any unreported defect or deficiency and for any consequential damage, property damage, or personal injury of any nature.”

(5) As a backup, another clause provided that if TFB is found liable under any theory of recovery, “liability . . . shall be limited to a sum equal to the amount of the fee paid . . . for the inspection and report.”

b. The court affirms the trial court’s grant of summary judgment to TFB finding that the inspection contract was unambiguous and Santana had failed to introduce any evidence to establish a material issue of fact regarding her unconscionability claim.

c. Santana also sued the seller and the seller’s real estate agent alleging negligence, fraud, and KCPA violations.

(1) However, the purchase contract contained a mediation clause which required “[a]ny dispute” to be “submitted to mediation in accordance with the rules and procedures of the Homesellers/Homebuyers Dispute Resolution System.”
The clause expressly included disputes concerning disclosure, or non-disclosure, of information relating to the condition of the house being sold.

Santana nevertheless filed suit, the defendants answered and asserted the failure to mediate as a defense, and Santana subsequently filed a motion to compel mediation.

d. In response to Santana’s motion, the defendants filed a motion to dismiss which the trial court granted.

The Court of Appeals affirms the trial court’s actions holding the clause, although not explicit on the matter, clearly implied that mediation was a condition precedent to pursuing remedies through litigation.

As Judge Greene observes in his opinion:

“There is no middle ground: mediation cannot effectively and fully serve its purpose of alternative resolution unless attempted prior to suit.”

Under these circumstances the trial judge properly dismissed the action.

e. The court’s holding in Santana lends support to a number of contractual techniques that may be used to have the parties confer with one another before they sue one another.

For example, an obligation to provide the other contracting party with notice of an alleged breach, and a period of time to address the matter before suit can be filed, is a type of mediation clause because it allows the parties to talk, explain, clarify, negotiate, and hopefully settle their disputes.

Although the ability to immediately sue the other party may have been jealously preserved in the past, today contract
clauses that require or allow the parties to confer before suing are viewed favorably by the courts.


1. As part of a divorce settlement, Margaret Law, in the late 1970s, entered into various agreements with business entities under the control of her ex-husband.

2. The agreement at issue is a Financing Agreement ("FA") that Margaret entered into in 1984 to establish her economic interests in a real estate project to construct a new corporate headquarters for The Law Company.
   a. The FA gave Margaret an 11% "equity participation" in the new building which had apparently paid her $2.25 million from 1984 through 2004.
   b. The FA also gave her 11% of the proceeds upon liquidation when Law Company Building Associates, a limited partnership, terminated in 2004, or was earlier dissolved or the building sold.

3. The current dispute arose when the general partner for Associates took the necessary action to extend the statutory life of the limited partnership from 2004 to 2024. The Law entities took the position that there was no obligation to liquidate until 2024, or earlier if Associates was dissolved.
   a. Margaret sued asserting claims under the FA for breach of contract, breach of an implied covenant of good faith and fair dealing, and reformation.
   b. Her basic complaint was that the Law entities had an obligation to liquidate and pay her 11% of the proceeds in 2004.

4. The trial court dismissed Margaret’s lawsuit stating it was barred by the statute of limitations.
5. A majority of a Court of Appeals panel reverse and send the case back to the trial court to reconsider the statute of limitations issues.

6. The most significant ruling by the court is that a different accrual date can apply to a reformation cause of action when the underlying instrument is a contract instead of a conveyance.
   
a. For conveyances the cause of action for reformation due to mistake begins when the deed is executed.

b. The court holds that for contracts a reformation cause of action does not accrue until the mistake is discovered, or with reasonable diligence could have been discovered.

c. In this case the contract was entered into over 25 years ago and now most of the people who could offer testimony concerning the agreement are dead, including Margaret’s ex-husband; Margaret is 83.

d. The court does not discuss any of the inherent complications regarding reformation, such as reliance on the undisturbed document by investors, creditors, and other third parties.

7. One disturbing aspect of the court’s discussion is its characterization of the obligation of good faith, relying upon what has been charitably described as one of the most baffling contract decisions of the Kansas Supreme Court: *Kansas Baptist Convention v. Mesa Operating Limited Partnership*, 253 Kan. 717, 864 P.2d 204 (1993). See David E. Pierce, *The Renaissance of Law in the Law of Oil and Gas: The Contact Dimension*, 42 WASHBURN L. J. 909, 920-23 (2004). The court observed:

   “Contrary to the argument advanced by defendants, a party can breach this implied covenant absent a specific covenant to which it must apply. In fact, our Supreme Court has noted that Kansas courts will impose an obligation of good faith that would override express contract terms, except in the area of employment-at-will.”

a. This statement is hard to reconcile with the basic concept that a court
will not imply a covenant when there are express contract terms that address the matter.

b. It is likely the court intended to say that to the extent the express contract terms give a party discretion in performance or enforcement of the contract, the party must exercise its discretion in good faith so as to carry out the underlying intent of the parties – as revealed by the express terms of the contract.

c. Reliance by the majority on such a broad statement of the implied covenant of good faith, and the Kansas Baptist Convention case, are best explained by Judge Pierron’s observation in his dissenting opinion:

“The essential fact is that Margaret Law was not to get her share of the real estate until there was a sale or refinancing of the property. As things have worked out, it has not been to the economic advantage of Law Company Building Associates and the Law Company to refinance or sell the property. In fact, such may well not occur in the near future and before the life span of Margaret Law ends. Essentially, the majority does not think this is fair.” (Emphasis added).

d. This is perhaps best revealed by the majority opinion when it notes the circumstances of Margaret are “remarkably similar” to those in Kansas Baptist Convention, a notoriously result-driven case.

8. Whether based upon the express contract terms, or an implied contract term arising from the express terms, the statute of limitations would accrue when the contract was breached, not when it was entered. In this case the court found the alleged breach occurred in 2005 and under the applicable 5-year statute of limitations Margaret’s lawsuit was timely.
III. PROPERTY LAW

A. Ownership Concepts and Remedies


   a. Water District looking for water sources and sought a temporary easement to enter Shipe’s land to conduct test drilling in search of water. Permission was denied and the Water District sought to condemn the necessary easement. The trial court granted the requested easement and the Shipes filed this separate action for injunctive relief.

   b. The basis for the Shipe’s objection was that without a permanent access to the point of diversion, the Water District could not obtain any water rights. Since the Water District does not own any water rights, and does not own a permanent right to make a diversion, the district court saw no reason to allow a temporary easement to look for water.

   c. The Supreme Court notes the Water District does not need to own a water right in order to obtain a temporary easement to search for water under its authorizing statutes.

   d. The issues raised regarding the Water District’s ability to obtain a water right is not ripe because the District may never decide to seek a water right.

   e. The Shipes lack standing to complain about any sort of taking regarding water rights because they currently have no water rights in their property.

   f. Court notes the following basic rules of property in water:

      (1) “[T]he Kansas Legislature established that a water right,
whether vested or appropriated, 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) “[A] water right does not constitute ownership of the water itself; it is only a usufruct, a right to use water.”

(3) “[T]he KWAA [Kansas Water Appropriation Act] dedicates water resources to the use of the public, prohibits water rights in excess of the reasonable needs of the appropriators, and subjects water rights to the principle of beneficial use.”

(4) “The effect of these principles is that the Shipes do not own the rights to the water appurtenant to their land simply because they own the land. To hold water rights, they must have applied for and been granted the rights.”

2. Court discusses basic ownership rights in produced natural gas that has been placed into a gas storage reservoir. *Northern Natural Gas Co. v. Martin, Pringle, Oliver, Wallace & Bauer, L.L.P.*, 289 Kan. 777, 217 P.3d 966 (2009).

a. The U.S. District Court for the District of Nebraska certified the following question to the Kansas Supreme Court:

“Does an injector of natural gas into underground storage, who demonstrates such gas was originally injected into underground storage but migrated to adjoining property or to a stratum or portion thereof which has not been condemned as allowed by law or otherwise purchased, lose title to or possession of the migrated gas when the gas migrated before July 1, 1993, the effective date of the controlling statute, Kan. Stat. Ann. §§ 55-1210, and was not captured or reduced to possession by another prior to July 1, 1993?”

b. The proceeding in the Nebraska federal court concerns a legal
malpractice action by Northern against its former legal counsel, Martin Pringle, associated with a jury instruction which Northern asserts Martin Pringle failed to object to at trial. The instruction states:

“Question 1: On or after July 1, 1993, did Northern’s stored gas migrate to the area of the ‘No. 1 Park’ and ‘No. 1 Park A’ wells?”

(1) The jury answered “no.”

(2) The focus of Northern’s complaint was that the jury instruction was an inaccurate statement of the law and Northern was damaged when its counsel failed to object and preserve the issue for appeal.

(a) Had the jury answered “yes” presumably it would have operated in Northern’s favor. Depending upon the evidence offered at trial, and the level of confusion surrounding the issues, the jury question might have been of some benefit to Northern.

(b) However, the Nebraska federal court believed that if the instruction was an accurate statement of the law, then presumably there could be no harm to Northern when its counsel failed to object to an instruction the Kansas Supreme Court has indicated was proper.

c. The Court’s focus is on §(c) of 55-1210 which states, in part:

“With regard to natural gas that has migrated to adjoining property or to a stratum, or portion thereof, which has not been condemned as allowed by law or otherwise purchased:

(1) The injector . . . shall not lose title to or possession of such gas if such injector . . . can prove by a preponderance of the evidence that such gas was originally injected into the underground storage.”
d. K.S.A. § 55-1210 was passed in 1993, and took effect on July 1, 1993, to respond, in part, to the Kansas Supreme Court's opinion in *Anderson v. Beech Aircraft Corp.*, 699 P.2d 1023 (Kan. 1985), which applied the rule of capture to gas that migrated to lands not subject to the injector's storage rights. K.S.A. § 55-1210 provides:

55-1210. Property rights to injected natural gas established. (a) All natural gas which has previously been reduced to possession, and which is subsequently injected into underground storage fields, sands, reservoirs and facilities, whether such storage rights were acquired by eminent domain or otherwise, shall at all times be the property of the injector, such injector's heirs, successors or assigns, whether owned by the injector or stored under contract.

(b) In no event shall such gas be subject to the right of the owner of the surface of such lands or of any mineral interest therein, under which such gas storage fields, sands, reservoirs and facilities lie, or of any person, other than the injector, such injector's heirs, successors and assigns, to produce, take, reduce to possession, either by means of the law of capture or otherwise, waste, or otherwise interfere with or exercise any control over such gas. Nothing in this subsection shall be deemed to affect the right of the owner of the surface of such lands or of any mineral interest therein to drill or bore through the underground storage fields, sands, reservoirs and facilities in such a manner as will protect such fields, sand, reservoirs and facilities against pollution and the escape of the natural gas being stored.

(c) With regard to natural gas that has migrated to adjoining property or to a stratum, or portion thereof, which has not been condemned as allowed by law or otherwise purchased:

(1) The injector, such injector's heirs, successors and assigns shall not lose title to or possession of such gas if such injector, such injector's heirs, successors or assigns can prove by a preponderance of the evidence that such gas was originally injected into the underground storage.

(2) The injector, such injector's heirs, successors and assigns, shall have the right to conduct such tests on any existing wells on adjoining property, at such injector's sole risk and expense including, but not limited to, the value of any lost production of other than the injector's gas, as may be reasonable to determine ownership of such gas.

(3) The owner of the stratum and the owner of the surface shall be entitled to such compensation, including compensation for use of or damage to the surface or substratum, as is provided by law, and shall be entitled to recovery of all costs and expenses, including reasonable attorney fees, if litigation is necessary to enforce any rights under this subsection (c) and the injector does not prevail.

(d) The injector, such injector's heirs, successors and assigns shall have the right to compel
compliance with this section by injunction or other appropriate relief by application to a court of competent jurisdiction.

(1) §(c) is the specific portion of 55-1210 which addresses the Anderson capture rule by allowing the injector to avoid the rule of capture once it is able to establish, "by a preponderance of the evidence," that "such gas was originally injected into the underground storage."

(a) This was what Northern was attempting to do in its case against Trans Pacific Oil Corporation.

(b) In light of the jury’s negative answer to Question 1, Northern apparently failed to carry the burden necessary to establish that "such gas [beneath and produced from Trans Pacific’s land] was originally injected into the underground storage."

(2) Another temporal issue regarding §(c) is whether the producing party, on adjacent lands, is liable for gas it produces from its land prior to a determination that "such gas was originally injected into the underground storage."

(a) Will the finding apply to all gas in-place at the time of the requisite "preponderance of the evidence" conclusion?

(b) Will it also apply to gas already produced by the third party prior to the "preponderance of the evidence" conclusion?

e. The ownership status of the gas in this case is stated by the Court as follows:

"Given that Northern did not obtain a certificate to condemn the adjacent landowner’s property prior to July 1, 1993, the adjoining landowners possessed a right, title, and interest in and to the gas which had migrated to the adjoining property as of that date."
The Court answers the certified question by noting that K.S.A. §55-1210 has only prospective effect as of July 1, 1993, and therefore:

"[P]rior to July 1, 1993, the landowners adjoining Northern's underground gas storage area possessed the legal right to produce and keep the injected gas which had migrated onto their property, unless and until Northern obtained a certificate to expand its storage area onto their land and paid them for that privilege through a condemnation action. K.S.A. 55-1210 abolished that right [the Anderson self-help capture rights], as well as permitting migrating gas to trespass upon adjoining land [because it is no longer subject to the rule of capture]. Such a substantive change to vested rights cannot apply retroactively."

g. The real remedy for dealing with injected gas that migrates into adjacent, uncontrolled lands, is revealed by the Court in Union Gas System, Inc. v. Carnahan, 774 P.2d 962 (Kan. 1989). You condemn it.

(1) The Court in Union Gas noted that after trying to obtain a storage lease from the DeTars (Carnahan's oil and gas lessors) since 1954: "[O]n March 11, 1986, Union finally decided to exercise its right as a natural gas public utility to condemn the DeTar subsurface for its use in underground storage."

(a) This was after, however, Carnahan had drilled wells on the DeTars land and was producing large volumes of gas, which was ultimately determined to be at least 82% injected gas attributable to Union's storage activities.

(b) The gas produced by Carnahan was ultimately produced and sold to Union which it in turn injected into the storage reservoir.

(c) As Justice Herd, writing for the Court in Union Gas noted: "This created a clever circle of purloined production, and a successful one under the rule of capture as stated in Anderson."

(2) Arguably, a major limitation imposed by Union Gas on the producer's Anderson rights, is the Court's holding that the
landowner need only be compensated for "native gas" beneath their property.

(a) Under Anderson, along with Kansas ownership-in-place concepts, the adjacent landowner would argue they are entitled to all the gas that is in-place beneath their property as of the date the condemnation process is triggered.

(b) An interesting aspect of the Northern Natural holding is whether the landowner should be credited, in a condemnation proceeding, with gas in place as of July 1, 1993.

(3) A related issue is whether, in light of Anderson and K.S.A. §55-1210(c), the term "native gas" under the condemnation statutes should be interpreted as the gas remaining in the property at the time of condemnation?

(a) However, the pre-K.S.A. §55-1210 statement in Union Gas is pretty clear:

"Cross-appellants argue, pursuant to Anderson, that they should be compensated for the value of injected gas as well as native gas under the property. The legislature has specified, however, only that native gas be considered. See K.S.A. 55-1201(c), K.S.A. 55-1204(a)(2), and K.S.A. 55-1205. Thus we reject cross-appellants' argument and find no error by the Commission."

[NOTE: these statutes were in existence, in one form or another, as early as 1951 and are a distinct set of statutes from K.S.A. §55-1210.]

(b) Also, since K.S.A. §55-1210(c)(3) provides for compensation "for use of...the substratum," it can be argued that although there will be no compensation for the injected gas (that the utility can carry its burden of proof is not native gas), there will be compensation for use of the space to store the non-native gas.
(c) Even the Court in *Union Gas* held the injector was obligated to account for “a reasonable rental for the use of the DeTars’ land.”

h. When K.S.A. §55-1210 was passed to negate the rule of capture remedy provided by *Anderson*, this development, combined with the native-gas-only compensation rule recited in *Union Gas*, probably led operators of gas storage facilities to believe that they no longer needed to worry about activities around their facilities.

(1) It simply would not be economic for surrounding landowners, and their lessees, to try and drill into a storage reservoir.

(2) Nor would it be likely that landowners would seek compensation for use of subsurface pore space that they are not able to use themselves and in any event would require considerable expert evidence to establish their case.

(3) So, perhaps the passage of K.S.A. §55-1210 would eliminate the need to condemn? Not so. It has done just the opposite by triggering the need for condemnation at the earliest point in time possible.


(1) From this the court of appeals concludes that Schonthaler owned the land and “Dick Properties owns all mineral interests in the land.”

(2) Dick Properties therefore retained the benefits as the lessor under a 1988 oil and gas lease with the current working interest owner of the oil and gas lease: Paul Bowman Oil Trust (“Bowman”).

(3) Bowman sought to renew a saltwater disposal agreement that would allow it to dispose of salt water from the leased land
and from other lands.

(4) The disposal agreement provides for disposal of salt water into the

b. The issue: who must Bowman contract with for saltwater disposal
   rights that extend beyond those encompassed by its rights as an oil
   and gas lessee?

   (1) The surface owner only (Schonthaler)? The mineral owner
       only (Dick Properties)? Both the surface owner and mineral
       owner?

   (2) The parties stipulated that the disposal of water under the
       disposal agreement did not impact the oil and gas rights of
       Dick Properties.

   (3) Held: The surface owner, Schonthaler, owns the rights to
       dispose of things on the property that do not impact oil and
       gas operations—therefore Bowman need not contract with the
       mineral owner (Dick Properties).

c. Analysis: “We do not think Dick Properties retains sufficient interest
   in this real estate that would require it to be a party to a saltwater
   disposal lease. . . . In our view, what Dick Properties reserved was
   simply the mineral interests to the real estate.”

   (1) Court examines the mineral interest retained by Dick
       Properties as though it was merely the rights to oil and gas.

   (2) Would the outcome be different if indeed Dick Properties
       owned “all” the minerals in the land—not just the oil and gas?

   (3) Court concludes Dick Properties lacked the ability to use its
       mineral interest to authorize the disposal of salt water
       produced off premises.

   (4) Conclusion: “Therefore, we hold Dick Properties transferred
       the rights to the saltwater disposal agreement to Schonthaler
       by execution of the deed.”

a. Progressive Products, Inc. ("PPI") manufactures and sells a ceramic coating for pipe elbows known as Ceram-Back. VIN Manufacturing, LLC ("VIN") was formed by persons who were formerly employed by PPI. VIN was created to compete with PPI by offering coating services using PPI's formula for Ceram-Back.

b. PPI sued VIN and the other participants asserting they misappropriated PPI's trade secrets regarding Ceram-Back.

c. The district court found that PPI had "a trade secret that included the Ceram-Back formula, mixing process, the pricing method contained in the computer program, and the price sheet . . . ." The district court entered an injunction against VIN ordering it to pay PPI a 20 percent royalty on sales occurring between July 21, 2006 through July 20, 2009.

   (1) PPI appealed arguing the court should have imposed a permanent injunction against any use of PPI trade secrets.

   (2) VIN cross-appealed arguing there was insufficient evidence to support that PPI had a trade secret to misappropriate.

d. First inquiry, under the Kansas Uniform Trade Secrets Act ("KUTSA"), did PPI have a trade secret to protect?

   (1) K.S.A. § 60-3320(4) defines "trade secret" as:

   (4) "Trade secret" means information, including a formula, pattern, compilation, program, device, method, technique, or process, that:

      (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and

      (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.
(2) The parties agree that under appropriate circumstances customer lists, price lists, computer programs, Ceram-Back formula, and the mixing and application process can all be a “trade secret” under 60-3320(4)(i).

(3) The matter in dispute is whether PPI took the “efforts that are reasonable under the circumstances to maintain its secrecy.”

e. The court analyzes each asserted trade secret to determine whether PPI took the “efforts that are reasonable under the circumstances to maintain its secrecy.”

(1) Ceram-Back formula. Yes. Although PPI posted an MSDA sheet listing the product’s ingredients, PPI took actions to prevent employees from disclosing the formula to the public.

(2) The mixing process. No. “PPI points to no proof that it treated this information with any secrecy, and no such evidence could be found in the record.”

(3) The batch method of determining the volume of product required for a job. Yes. Although it was possible for an employee to calculate the product volume associated with the batch method, “KUTSA only requires efforts to maintain secrecy that are reasonable under the circumstances; perfection is not required.”

(4) Price lists. No. These were disclosed to any customer who requested them. “Thus, as a matter of law, the price sheets did not constitute trade secrets, and the district court erred in holding otherwise.”

(5) Customer lists. No. This was not addressed by the trial court.

f. Because the Ceram-Back formula and the batch method constituted trade secrets, the court must review whether they were misappropriated by VIN.

(1) K.S.A. § 60-3320(2) defines “misappropriation” as:
(2) "Misappropriation" means:

(i) acquisition of a trade secret of another by a person who knows or has reason to know that the trade secret was acquired by improper means; or

(ii) disclosure or use of a trade secret of another without express or implied consent by a person who

(A) used improper means to acquire knowledge of the trade secret; or

(B) at the time of disclosure or use, knew or had reason to know that his knowledge of the trade secret was

(I) derived from or through a person who had utilized improper means to acquire it;

(II) acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or

(III) derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or

(C) before a material change of his position, knew or had reason to know that it was a trade secret and that knowledge of it had been acquired by accident or mistake.

(2) K.S.A. § 60-3320(1) defines “improper means” as:

(1) "Improper means" includes theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, or espionage through electronic or other means.

The facts supported a finding that VIN employees obtained the Ceram-Back formula, and the batch method information, from PPI and used it in their operations.

Remedy: K.S.A. § 60-3321 addresses the remedies for misappropriation of a trade secret as follows:

(a) Actual or threatened misappropriation may be enjoined. Upon application to the court, an injunction shall be terminated when the trade secret has ceased to exist, but the injunction may be continued for an additional reasonable period of time in order to eliminate commercial advantage.
that otherwise would be derived from the misappropriation.

(b) In exceptional circumstances, an injunction may condition future use upon payment of a reasonable royalty for no longer than the period of time for which use could have been prohibited. Exceptional circumstances include, but are not limited to, a material and prejudicial change of position prior to acquiring knowledge or reason to know of misappropriation that renders a prohibitive injunction inequitable.

(c) In appropriate circumstances, affirmative acts to protect a trade secret may be compelled by court order.

1. The trial court relied upon subsection (b) to order payment of a royalty.

   (1) The facts do not support application of subsection (b) because there are no “exceptional circumstances” to warrant letting VIN to continue using the misappropriated trade secrets.

   (2) There is no public interest nor any equitable consideration that would justify allowing VIN to be given the benefit of the royalty remedy.

   (3) The court remands for the trial court to consider an appropriate remedy under subsection (a) of 60-3321.

   (4) Regarding the duration of any prohibitory injunction, the court quotes the comment to the Uniform Trade Secret Act which states:

   “Subject to any additional period of restraint necessary to negate lead time, an injunction accordingly should terminate when a former trade secret becomes either generally known to good faith competitors or generally knowable to them because of the lawful availability of products that can be reverse engineered to reveal a trade secret.”

   (5) The court’s interpretation of this comment is as follows:

   “The injunctive relief ordinarily should continue only until the defendant could have acquired the information by proper means. Injunctions extending beyond this period are justified only when necessary to deprive the defendant of a head start
or other unjust advantage that is attributable to the misappropriation. . . . More extensive injunctive relief undermines the public interest by unduly restraining legitimate competition.”

5. **Court allows reformation of deed to remedy parties’ mutual mistake as to land being conveyed.** *Unified Government of Wyandotte County/Kansas City v. Trans World Transportation Services, L.L.C.*, 227 P.3d 992 (Kan. Ct. App., March 26, 2010).

a. Wyandotte County (WC), in 1997, leased land to Trans World. The land was part of an 8.95-acre parcel where, in 1989, WC built a fire station occupying 2.58 acres of the land, with an address of 444 Kindelberger Road. The remaining 6.45-acre tract contained a 27,164 square-foot building with an address of 420 Kindelberger Road and a mailing address of 400 Kindelberger Road. The two tracts were never formally separated by deed or other action.

b. In the lease to Trans World the leased area was described as: “One Building and Improved Grounds located at 420 Kindelberger Road, Kansas City, Kansas, consisting of a total of 280,962 square feet or 6.45 acres (+/-), with a 27,164 square feet building . . . .”

c. A dispute arose between the parties and as settlement WC agreed to convey to Trans World the leased land. The WC resolution authorized issuance of a deed conveying the property at 400 Kindelberger Road to Trans World.

d. When WC ordered title insurance the commitment referred, mistakenly, to the entire 8.95-acre tract. The same description was used in the warranty deed to Trans World.

e. When WC discovered the mistake, Trans World denied the mistake was mutual and demanded that WC either enter into a lease for the fire station or have the fire department move out within 30 days.

f. WC sued seeking reformation of the deed, due to mutual mistake, so that it covers only the 6.45-acre tract the parties intended to convey pursuant to their settlement agreement. Trial court held for WC, Trans World appeals asserting reformation was improper and, in any event, the boundary line drawn by the court for the reformed deed was improper.
g. HELD: Affirmed. The deed was properly reformed by the trial court.

h. Law of reformation mutual mistake. To prove mutual mistake concerning a written instrument, a party must prove, by clear and convincing evidence:

1. a prior agreement by the parties that the written instrument seeks to evidence;

2. that a mistake occurred in preparing the written instrument [as opposed to a mistake associated with the prior agreement the instrument seeks to evidence]; and

3. where there is no fraud or inequitable conduct by a party [which could allow for a unilateral mistake], that the mistake is mutual.

i. Other rules: Mutual mistake is not affected by a party’s negligence in failing to carefully examine the instrument.

j. Applied to the facts of this case:

1. Deed that is the object of the mistake was entered into to effectuate the parties’ prior settlement agreement.

2. Settlement agreement referred solely to the 400 Kindelberger Road property, not the fire station property. WC commissioners authorized conveyance of the 400 Kindelberger Road property.

3. It was clear the prior settlement agreement conveyed only the leased property and not the fire station.

4. “There is overwhelming evidence of the mutual mistake by the parties in delivering and accepting a deed inconsistent with their clear intention expressed in their unambiguous settlement agreement.”

k. Law of reformation for mutual mistake.

1. “When a mutual mistake is made in describing property in a deed and the instrument does not convey the property intended, the deed may be reformed to conform to the parties’
original intentions.”

(2) The grantor did not intend to convey the property and the grantee has no right to retain the property.

(3) “Under these circumstances, the court will step in to correct the mistake, provided that the grantor would be prejudiced by a failure to reform the deed, and the grantor’s position in equity is superior to that of the grantee.”

1. Court upholds the division of the lands and rejects TransWorld’s merger argument noting that merger is a matter of intent and the mutual mistake demonstrates the parties did not intend to merger the settlement agreement into the erroneous deed.


a. Bitner asserts it is the owner of a reversionary interest in land in which an easement for a railroad tract was granted to Watco’s predecessor-in-interest in 1889. Bitner argues the right-of-way has been abandoned so that Bitner’s land is no longer burdened by the easement. Apparently a football field and track have been built on the lots burdened by the easement.

b. Watco raises two defenses. First, that it owns the land in fee so it cannot be abandoned. Second, that even if all it owns is an easement, the only way it can be abandoned is by following the abandonment procedure administered by the federal Surface Transportation Board.

c. The trial court, and the court of appeals, each hold that in order to abandon a railroad right-of-way it can only be done with approval by the appropriate federal (49 U.S.C. § 10903) or state (K.S.A. § 66-525) authority.

d. The court suggests Bitner’s remedy is to pursue an abandonment with the Surface Transportation Board.

e. Arguably 49 U.S.C. § 10903 and K.S.A. § 66-525 should be limited to situations where the railroad seeks to abandon its service obligation as a public utility. The court in this case seeks to burden the private property owner’s reversionary interest – established in
1889 – with regulatory obligations created a century after the basic property rights of the parties were established.

(1) Arguably, as a matter of state property law, the railroad’s easement will terminate once it ceases using the land for the rights encompassed by the easement.

(2) The reversion is automatic once the intent to abandon exists – without regard for regulatory limitations.

f. The court’s holding fits nicely with the Rails-To-Trails program designed to allow a public interest group to take control of the reversionary interest for public trails – a program which has its own “takings” problems.

B. Property and Tort: Conversion and Negligence


a. MidFirst foreclosed on Snider’s house in Dighton, Kansas. Snider was served with notice of the foreclosure at her home in Healy, Kansas. Following the foreclosure, and the redemption period, MidFirst hired Safeguard Properties, Inc., who in turn hired Donald Rolison to take possession of Snider’s personal property that was left at the Dighton house. The property was gathered, and inventoried, under a writ of assistance with the sheriff.

b. Rolison ultimately disposed of the property in a garage sale for $500.

c. All notices concerning the seizure and sale of the property were sent to Snider’s Dighton address when MidFirst was aware of Snider’s Healy address. Snider did not receive any of the notices. Snider inquired of the sheriff’s department about the whereabouts of her property and was told they did not know who had it.

d. The court of appeals reverses the trial court’s grant of summary judgment against Snider because Snider had standing to assert rights in her property and there were properly controverted issues of fact that made summary judgment improper.

e. Snider also sought to assert her son’s conversion claims but the court
holds the son’s attempt to assign his conversion claims, which are claims in tort, are not assignable in Kansas.

f. The court notes that since there was no proper authority to sell Snider’s property, this could constitute a conversion of the property, citing Restatement (Second) of Torts § 228 which provides:

“One who is authorized to make a particular use of a chattel [for example the initial taking of the property from the Dighton residence under the writ of assistance], and uses it in a manner exceeding the authorization [for example, selling it without proper authority], is subject to liability for conversion to another whose right to control the use of the chattel is thereby seriously violated.”

g. The court also notes that on remand the trial court should consider K.S.A. §§ 84-7-209 and 210 regarding enforcement of a warehouseman’s lien.

2. Oil and gas developer properly given judgment against negligent abstractor hired by developer’s attorney to prepare certificate of title so attorney could provide his producer client with a drill site title opinion. *Southwind Exploration, LLC v. Street Abstract Co., Inc.,* 42 Kan. App.2d 122, 209 P.3d 728 (2009), review withdrawn (Sept. 28, 2009).

a. Abstractor was instructed by attorney to prepare a “certificate of title” on a defined tract of land, but also instructed them as follows:

“[Y]ou will need to go back to the last oil & gas lease prior to this one.”

b. The attorney’s client, Southwind, had obtained an oil and gas lease and wanted a drilling title opinion.

(1) Certificate of title failed to identify an undivided one-half mineral interest owned by Union Central Life Insurance Company and leased to another oil company.

(2) The attorney relied on the certificate of title to prepare his title opinion, which Southwind relied upon in drilling four wells on the lease it had covering only one half of the mineral interest.

c. Southwind sued the abstract company, in tort, relying upon the
Restatement (Second) of Torts § 552 which states:

“(1) One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.

“(2) Except as stated in Subsection (3), the liability stated in Subsection (1) is limited to loss suffered

“(a) by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it;

“(b) through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.

“(3) The liability of one who is under a public duty to give the information extends to loss suffered by any of the class of persons for whose benefit the duty is created, in any of the transactions in which it is intended to protect them.”

d. “Southwind claimed Street was negligent in failing to examine the records of the county treasurer and county register of deeds to identify Union Central’s interest and in supplying false information for the guidance of Southwest [sic] and Lacy [Southwind’s attorney] regarding the ownership of mineral interests in the property.”

(1) Jury assessed no fault to Southwind, 70% to Street, and 30% to Lacy.

(2) Southwind’s 70% of the $329,043.47 in damages was $230,330.43.

e. Held: Affirmed.

(1) No case authority on abstractor obligations regarding a “certificate of title.”
(2) Regarding preparation of an abstract of title, the Kansas Supreme Court has held:

“In Kansas, an abstractor is liable for all negligent errors and omissions not only to his or her employer but to all persons who purchase or invest in land relying on an abstract furnished for that purpose and without regard for privity.”

(3) Here the abstractor had a duty to Southwind, as someone within the “limited group” under the Restatement, to review the public records relating to the status of title to the property in a nonnegligent fashion.

(4) Even under the attorney’s limited instructions, and consistent with the abstractor’s certification, the abstractor fails to examine the county treasurer’s records which would have revealed Union Central’s mineral interest.

(5) “Clearly, a certificate of title is not an abstract of title. However, this does not explain or excuse Street’s failure to find and disclose Union Central’s interest for which there was evidence in the county’s public records during the time period of the search defined by the note from Lacy’s secretary.”


a. Evenson owned 160 acres which included some outbuildings and shade trees. The neighbor was conducting a controlled burn on its property, which became uncontrolled, and burnt up trees and outbuildings on the Evenson property.

b. Evenson wants $300,000+ to replace the damaged trees; Lilley wants to pay the difference between the fair market value of the land before and after the fire: $4,687 (which included the depreciated value of the buildings too).

c. Evenson argued the damage was temporary and therefore the cost of remediation should be the measure of damages – and if damages are limited to the fair market value of the land – then damages would be $160,000.
d. Lilley argued the damage was permanent and therefore should be measured by the difference in fair market value before and after the fire.

e. The district court rules the damage was permanent and awarded damages of $7,687.

f. Court of appeals notes the purpose of any measure of damages is to compensate the injured party for their injury.

g. The court notes that in some situations where you can show that trees had an independent value that is proven, recovery may be obtained for the loss of that value.

(1) This is not a replacement value analysis. Although Evenson presented evidence of what it would cost to replant big trees, it offered no evidence as to the distinct value of the big trees to the property – that was lost by the damage.

(2) “In light of the lack of evidence demonstrating the value of the trees destroyed by the fire, the proper measure of damages is the difference between the market value of the property before and after the fire.”

h. The court referred to the Evenson’s restoration cost figure of $307,999 as “patently unreasonable.”

C. The Inadequacies of Joint Tenancy

1. Joint tenancy can be a deceptively fragile relationship on which to plan a future. In re Kasparek, BAP No. KS-09-041, 426 B.R. 332, 2010 WL 1270341 (B.A.P. 10th Cir. April 5, 2010).

a. The trustee in bankruptcy commenced a Bankruptcy Code 11 U.S.C. § 363(h) proceeding to sell all rights in the land in which Jonathon held legal title to a 1/3rd undivided interest as a joint tenant with his brother James and his father Wayne.

b. When the requirements of § 363(h) are met the trustee can sell 100% of the jointly held property in order to maximize the value of the debtor’s undivided interest in the property.

c. The non-debtor joint owners are forced to sell their interests; if they
want to keep the land, they have to be the successful bidders at the sale.

d. Separate from the right to sell Jonathon’s 1/3rd interest, a preliminary issue is whether Jonathon really owns a 1/3rd interest when it can be proven: the father paid all the purchase price, manages the property as his own, and intended the joint tenancy merely as an estate planning tool – with no intent to make a present gift of the interest to either of the two sons.

e. In the past, Kansas courts have been willing to look behind the recorded document to ascertain the true intent of the parties to the conveyance – even though there is nothing ambiguous about the deed. Opportunity for courts to practice some equity to protect the party contributing the money – typically from a child’s creditor.

(1) Part of this willingness may be the product of applying bank account and other personal property joint tenancy law to the real property context.

(2) This is understandable since K.S.A. § 58-501 applies to “[r]eal or personal property granted or devised to two or more persons . . . .”

(3) However, the world of personal property does not operate under the real property recording laws, such as K.S.A. § 58-2221 (2005) (providing for recording of “[e]very instrument in writing that conveys . . . [r]eal estate . . . or . . . whereby any real estate may be affected . . . .”) and K.S.A. § 58-2222 (2005) (recording imparts “notice to all persons of the contents thereof; and all subsequent purchasers and mortgagees shall be deemed to purchase with notice.”).

(4) But, personal property often operates under its own unique bodies of law, such as the Uniform Commercial Code. E.g., Bridges v. Central Bank and Trust Co., 926 F.2d 971 (10th Cir. 1991) (certificate of deposit owned by five individuals in “or” form, and held in joint tenancy, could be pledged by any one of the five and allow the creditor to receive 100% of the proceeds upon default; relying upon UCC § 3-116(a) and § 9-1205).

f. The court in Kasparek explores the precise basis for allowing a court
to look behind the recorded document and holds that in Kansas the theory is based upon an implied trust which implicates statutes that specifically address the concept in real estate transactions.

(1) K.S.A. §§ 58-2401 to 58-2408 (2005), is an act, that took effect in 1868, to address the use of trusts in land to defraud creditors.

(2) Under the facts the father Wayne had the burden to establish that his son Jonathon had an agreement to hold the property in trust for the father.

(3) The court proceeds under the assumption Wayne was able to show an agreement that Jonathon held his interest in trust for his father – but then addresses the effect this unrecorded interest would have on a bona fide purchaser.

g. The court concludes: “The rights and powers of a bona fide purchaser include the right to obtain title to property free of certain unrecorded interests . . .” and, for purposes of the trustee's avoidance powers under 11 U.S.C. § 544, it is not necessary to have a transfer by the debtor to trigger the trustee's bona fide purchaser status.

h. The court's opinion does an excellent job of collecting and analyzing Kansas cases on a BFP's obligation to make inquiry of facts beyond the recorded document.

(1) Issue: to what extent must the trustee (BFP) make inquiry regarding the nature of the holdings by the three named joint tenants?

(2) Held: the joint tenancy deed establishes as a matter of law that the parties each owned an undivided one-third interest in the property and absent special circumstances triggering a duty to inquire beyond the deed, no duty exists – merely because the property is held in joint tenancy.

(3) The court reasons:

"We believe that a duty to inquire about the possibility of an implied trust or other unrecorded agreements when title is held by joint tenants undermines the purpose of the Kansas recording statutes, imposes an undue burden on purchasers,
and impairs the reliability of record title.”

2. The joint tenancy audit. A frequently over-looked issue upon death of a joint tenant is a study of events taking place under the joint tenancy relationship to determine whether it has, in fact, been severed so that the presumed deceased joint tenant is actually a cotenant that retains their undivided interest in their estate at death.

a. The risks here can be significant because if the joint tenancy was severed during the decedent’s lifetime, the decedent’s undivided interest will not go to the surviving joint tenant but will instead pass under the decedent’s will or intestate succession – or by other means, such as a transfer-on-death deed.

b. It is a high-risk proposition because it is generally “winner-take-all” meaning if there has been a “severance” of the joint tenancy the surviving joint tenants will take nothing from the decedent; the decedent’s heirs or devisees will take it “all.”

c. When the joint tenants entered into different oil and gas leases at different times (even though with the same lessee), did that act sever the joint tenancy and create a tenancy in common by operation of law?

(1) Issue has not been litigated in Kansas – probably because the prospect of a severance was not considered by anyone.

(2) The issue was recently the subject of litigation in Pennsylvania. In re Estate of Quick, 905 A.2d 471 (Pa. 2006) (no severance of the joint tenancy resulted because there was no “intent” to sever).

d. If one joint tenant enters into a mortgage will that cause a severance of their interest in Kansas?

(1) Because Kansas follows a “lien” theory of mortgages, as opposed to a “title” theory, it should not result in a severance because nothing has been conveyed to the mortgagee.

(2) However, we have problems with “dicta law” on this subject in Hall v. Hamilton, 667 P.2d 350, 354-55 (Kan. 1983), where the court stated:
“It is undisputed that any joint tenant may sever his or her joint tenancy interest in real property by ... mortgaging the joint tenancy interest ...”

(3) Although the statement in Hall was dicta, it was picked up as “law” in Hutchinson National Bank and Trust Co. v. Brown, 753 P.2d 1299, 1301 (Kan. Ct. App. 1988), rev. denied (June 22, 1988), where the court states:

“The Bank contends that the plain language in Hall requires Kansas courts to find that a pledge acts as a severance of the joint tenancy interest because there is no legal distinction in the operative effect of a mortgage or pledge (other than the type of property encumbered). We agree.”

(4) What does the governing statute say regarding the mortgage/pledge issue?

(a) The governing statute is K.S.A. § 58-501 (2005) which has been around since 1939 and is one of the few provisions of the 1939 Property Act that was given complete retroactive effect: “The provisions of this act shall apply to all estates in joint tenancy in either real or personal property herefore or hereafter created . . . .”

(b) The last phrase of K.S.A. § 58-502 makes it clear that the mere granting of a lien on property is not viewed as the severing event, but rather the foreclosure of the lien that results in a change of title through an actual sale of the interest:

“[N]othing herein contained shall prevent execution, levy and sale of the interest of a judgment debtor in such estate and such sale shall constitute a severance.”

(c) No court in Kansas has focused on this express language in the statute – at least not in the Hall or Hutchinson National Bank contexts.

(5) The mortgage issue, and even the pledge issue, remain open issues in Kansas.

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(a) K.S.A. § 58-502 takes the most appropriate approach to the issue by making an actual change of title to the encumbered interest the clear, defining event in which a severance will occur.

(b) Until a sale, and the resulting change in ownership, the joint tenancy would remain in effect. Not even the filing of a foreclosure action would cause a severance because no change in title will occur until the action has successfully run its course and a sale is completed.

(c) If a lender wants to protect itself from the winner-take-all aspects of joint tenancy, it should, as a condition to making the loan, require their borrower to sever the joint tenancy and convert it into a tenancy in common – unless, of course, the bank feels lucky and the borrower is the youngest and healthiest of the joint tenants.

3. Technical aspects of severance: “destroying” one of the “four unities.”

The “four unities” at common law required to create, and maintain, a joint tenancy are:

**Interest:** the tenants must have one and the same interest.

**Title:** the interests must accrue by one and the same instrument or conveyance.

**Time:** the interests must commence at one and the same time.

**Possession:** the property must be held by one and the same undivided possession.

a. If one of the “unities” is “destroyed,” or “lacking,” then the joint tenancy becomes a tenancy in common and the survivorship rights are eliminated.

b. Is it possible for a joint tenant to own less than an equal, undivided interest and still satisfy the unity of “interest” (tenants must have one and the same interest)? Not really – except, perhaps, in Kansas.

c. *In re Estate of Lasater,* 54 P.3d 511 (Kan. Ct. App. 2002), rev. denied (Dec. 17, 2002) (joint tenancy can be created when one joint
tenant is conveyed 99% and the other 1% – this does not, according to the court, violate the unity of interest). Lasater: right result, even though the unities analysis is open to challenge.

d. A strong argument can be made that courts need to abandon the unities analysis altogether.

(1) The unities analysis never fit the cases dealing with bank accounts.

(2) The Court of Appeals in Lasater properly focuses on the intent of the parties to resolve these issues. The intent was extremely clear in Lasater.

e. K.S.A. § 58-501 (2005) provides a statutory basis for abandoning the unities analysis and focusing on intent by providing:

“Real or personal property granted or devised to two or more persons including a grant or devise to a husband and wife shall create in them a tenancy in common with respect to such property unless the language used in such grant or devise makes it clear that a joint tenancy was intended to be created . . .”

D. The Latest Populist Uprising: Transfer on Death Conveyances of Interests in Real Estate and Motor Vehicles

1. The court in Kasparek offered the following thoughts:

“We also note that, by statute, Kansas permits interests in real property to be titled in a ‘transfer-on-death’ form, so that the estate planning attempted by Wayne could have been accomplished by designating directly on the deed the beneficiaries in whom the Property would vest upon his death. See Kan. Stat. Ann. § 59-3501. Such a designation may be changed or revoked without the consent of the beneficiary. Id. § 59-3503. The availability of transfer-on-death deeds in Kansas obviates the need to resort to a joint tenancy deed as an estate planning tool, and increases the reliability of land records. The fact that Kansas has such a statute further weighs against imposing a duty on purchasers to inquire of joint tenants regarding whether their interests are subject to a secret trust and were intended to vest only on death of one of the joint tenants.”

2. Kansas Statutes Annotated, Chapter 59, Article 35. – Transfer-On-Death


c. K.S.A. § 59-3512 (other nontestamentary transfers).

3. Addresses all the testamentary issues regarding an incomplete, totally revocable, gift. K.S.A. § 59-3507 (“A deed in transfer-on-death form 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.”).

4. The only formality required: the deed must be recorded. K.S.A. § 59-3501(a).

a. No delivery requirement.

b. Grantee/beneficiary need not be aware that the conveyance exists. K.S.A. § 59-3501(b).

5. The only unique limitation: cannot be “revoked by the provisions of a will.” K.S.A. § 59-5503(c).

6. No alternative beneficiaries stated in the deed, the gift will lapse if the designated beneficiary predeceases the grantor. K.S.A. § 59-3504(c).

7. Transfer-on-death conveyance by a joint tenant will not sever the joint tenancy; the transfer-on-death beneficiary will receive the interest only if the joint tenant grantor is the last surviving joint tenant. K.S.A. § 59-3505.

8. What follows is a drafting exercise, concerning Transfer-On-Death Deeds, given to my students at Washburn.
TRANSACTIONAL SKILLS
DRAFTING

Applying Legal Principles to Accomplish the Client’s Goals

Today among the most important estate planning tools are the durable power of attorney and transfer-on-death documents. Transfer-on-death documents are an improvement over the use of joint tenancy as a probate-avoidance tool because the donee does not currently receive an enforceable right in the property. This means the donee has no power over the property and the donor can change the deed at any time without the donee’s consent. If the donor fails to act, the property will pass to the currently listed donee at the donor’s death. Absent statutory authorization, these transfer-on-death arrangements would violate the Statute of Wills. (The Kansas version of the Statute of Wills is found at Kan. Stat. Ann. § 59-606 (2005)). Because the donor if free to change their mind, the gift is not complete until the donor dies. Until the donor’s death, they can alter the donee’s ability to receive the property.

This Exercise addresses the drafting of a transfer-on-death (“TOD”) conveyance. TOD conveyances are governed by Kan. Stat. Ann. §§ 59-3501 to 3507 (2005). However, you have a preliminary problem because the property being transferred is the right to receive a share of helium gas produced from wells drilled on land owned by Dock Hillard. In 1988 Dock received the interest described in the document labeled Exhibit A. Dock wants to use a TOD conveyance to transfer 76% of Dock’s helium rights to his son, Stephen Hillard.

Step One of the Drafting Process: Validation.

First Task: Prepare a one-page memorandum of law addressing whether the helium royalty Dock wants to transfer to Stephen is an “interest in real estate” as contemplated by Kan. Stat. Ann. § 59-3501(a) (2005). You can assume that unless the interest is a § 59-3501(a) “interest in real estate,” then the TOD procedures for “real estate” will not be available.


Third Task: Draft the TOD conveyance to transfer 76% of Dock’s helium royalty rights to Stephen.

Fourth Task: Draft a one page letter to Dock explaining what he needs to know about the TOD conveyance you have prepared. Dock has already asked you the following questions: (1) Do I have to give the TOD conveyance to Stephen? (2) Do I have to tell Stephen I have conveyed the interest to him? (3) After I sign and record the TOD conveyance to Stephen, can I later change my
mind and transfer the interest to someone else? (4) Can I use the value of the 76% interest covered by the TOD conveyance as collateral for a loan? (5) Can Stephen encumber the 76% interest by borrowing against it? Provide Dock with the information he will need to know in order to understand the rights created by his TOD conveyance to Stephen.

EXHIBIT A

STATE OF KANSAS  
COUNTY OF SHAWNEE  

Witnesseth that on this 10th day of June 1988 Forrest Hillard, as the owner of the following land in fee simple absolute: Section 3, Township 11 South, Range 15 East of the 6th Principal Meridian, in Shawnee County, Kansas (the “Land”); hereby conveys and warrants to Dock Hillard, for a term of 21 years from the date of this conveyance and so long thereafter as helium is produced from the Land, one-eighth of all the helium produced and saved from the Land.

FORREST HILLARD

Prepare the documents and deliver your final product to Shirley in Room 302 by Noon on March 10, 2006. Obtain your examination number for this Exercise #8 from Shirley.

As appropriate, apply the principles set out in Richard Wydick’s Plain English for Lawyers and the citation format specified in the “Practitioners’ Notes” portion of The Bluebook. All citations should be imbedded in the text of your work; no footnotes. Edit your work.
MEMORANDUM OF LAW

TO: File
FROM: David E. Pierce
DATE: 2 October 2006

I. QUESTION: Can the transfer-on-death (“TOD”) device under Kan. Stat. Ann. § 59-3501 (2005) be used to transfer the right to a share of helium produced from land?

II. ANSWER: Most likely. An interest classified as personal property for “oil and gas law” purposes can still be “an interest in real estate” for purposes of the TOD statutes.

III. DISCUSSION: The meaning of the phrase “an interest in real estate,” as used in Kan. Stat. Ann. § 59-3501(a) (2005), is a matter of statutory interpretation requiring application of Kan. Stat. Ann. § 77-201 (Supp. 2005), which provides: “In the construction of the statutes of this state the following rules shall be observed . . . Eighth. ‘Land,’ ‘real estate’ and ‘real property’ include lands, tenements and hereditaments, and all rights to them and interest in them, equitable as well as legal.” This adopts a broad interpretation of “real estate” without any limitation on how the rights at issue might be classified for “oil and gas law” purposes. The critical inquiry is to ascertain the “intent of the legislature” when it used the phrase “an interest in real estate” to define the permissible scope of the TOD device. Mitchell v. Liberty Mut. Ins. Co., 24 P.3d 711, 719 (Kan. 2001).

In Dubowy v. Baier, 856 F. Supp. 1491 (D. Kan. 1994), the court applies a similar analysis to define the phrase “interest in . . . real property” as used in Kan. Stat. Ann. § 60-1002 (2005) (quiet title statute). The court surveys various sources defining the phrase “interest in real estate” and notes: “Among property rights that have been found by courts to constitute an interest in real estate are leases, easements, rights to royalties, right to profits and ownership of mineral rights.” Id. at 1497 (emphasis added). This encompasses Dock’s helium rights which are one of the metaphorical “sticks” comprising the bundle of sticks that make up the “real estate.” Creation of the right requires a conveyance evidenced by a writing and administered under the recording acts. It is not similar to a transfer of a car or other item of tangible personal property that might be located on the land, instead it is a right, an interest, carved from land itself, “an interest in real estate.”

The TOD statutes have not been addressed by Kansas courts. [As of 2006] Although for oil and gas law purposes Dock’s helium interest could be classified as personal property, under certain circumstances it may also be classified as real property. See In re Sellens, 637 P.2d 483, 486 (Kan. Ct. App. 1981) (distinguishing “accrued” royalty from “unaccrued” royalty). Perhaps because of these inconsistent approaches, the court in National Bank of Tulsa v. Warren, 279 P.2d 262, 285-86 (1955), refused to apply oil and gas law classifications when evaluating whether conveyance of a production payment “affected” real estate under a mortgage registration tax statute. In Platt v. Woodland, 246 P. 1017, 1020 (Kan. 1926), the court, interpreting the scope of the term “estate” in a statute, holds the term was used as a “general” term, not a “technical” term and encompassed “whatever the grantor could convey . . . .” The phrase “interest in real estate,” if similarly interpreted as a “general” term, would include Dock’s helium interest that was carved out of the real estate.
TRANSFER-ON-DEATH DEED

Dock Hillard as owner ("Dock") transfers on death to his son, Stephen Hillard, as grantee beneficiary, the following described interest in real estate:

An undivided 9.50% of 100% of all the helium produced from: Section 3, Township 11 South, Range 15 East of the 6th Principal Meridian, in Shawnee County, Kansas (the "Land"), for a duration continuing until 10 June 2009 and so long thereafter as helium is produced from the Land.

THIS TRANSFER ON DEATH DEED IS REVOCABLE. IT DOES NOT TRANSFER ANY OWNERSHIP UNTIL THE DEATH OF DOCK. IT REVOKES ALL PRIOR BENEFICIARY DESIGNATIONS BY DOCK FOR THIS INTEREST IN REAL ESTATE.

Signed 6 October 2006.

DOCK HILLARD, Owner

ACKNOWLEDGMENT CERTIFICATE

Shawnee County, Kansas

This Transfer-On-Death Deed was acknowledged before me on 6 October 2006 by Dock Hillard.

DONNA K. HAVERKAMP
Notary Public
My Appointment Expires: _____________

Until notified otherwise, all tax statements that relate to the interest described in this Transfer-On-Death Deed should be sent to:

Dock Hillard, 1301 S.W. High, Topeka, Kansas 66604-1220.
Dear Dock:

Enclosed is the Transfer-On-Death Deed ("TOD" deed) you requested. Rights under a TOD deed are defined by several Kansas statutes. The TOD deed statutes apply to "an interest in real estate." This phrase is not defined and raises the issue whether a share of helium produced from land is "an interest in real estate." Complex classification principles create some risk the helium transfer could be challenged as not being an interest in real estate. My opinion is the statute will most likely be interpreted to include your helium interest. In the event I am wrong, it would mean the TOD deed to Stephen will not be given effect and the property will become part of your estate.

There are several things you should know about the Transfer-On-Death Deed rules in Kansas. First, the transfer will not have any effect at your death unless the deed is recorded with the Register of Deeds prior to your death. You do not have to give the deed to Stephen or even inform him that you have made the deed, although recording will make it a matter of public record. You can change your mind at any time during your life by conveying the property to someone else, or by following a simple statutory revocation procedure. However, you can not revoke the TOD deed by your Will. Although you do not hold the helium in joint tenancy, in the event you did, entering into this TOD deed would not sever or otherwise change your rights as a joint tenant. You will be able to deal with the interest covered by this TOD deed in any manner you desire during your lifetime. You can borrow against it and use it as collateral; it will be subject to the claims of your creditors and Stephen will take the property subject to any conveyances, liens, and other burdens occurring during your lifetime. If Stephen dies before you, his interest will lapse, which means the property will be part of your estate at your death. Although it is possible to designate alternative beneficiaries in the TOD deed, you have not chosen to do that in your deed. Stephen will not be able to borrow against, or otherwise encumber the property.

As a relatively new approach to disposing of property, it is important that if you ever decide to revoke the transfer, or make other dispositions of this property, please contact me so I can assist you by ensuring all statutory requirements are met. Let me know if you have any questions.

Sincerely;

David E. Pierce

DEP:dep
Enclosure: Transfer-On-Death Deed