MATTIONI, LTD.

COUNSELORS AT LAW

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Mattioni, Ltd., 399 Market Street, Suite 200, Philadelphia, PA 19106
www.mattioni.com firmmail@Mattioni.com (215)-629-1600

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Subsequent Purchasers Liable for Past Mortgage Despite Title Search

By Dawn M. Tancredi, Esquire

Benjamin Franklin created title insurance as indemnity against financial loss on real property due to title defects or liens. The first title insurance company was formed in Pennsylvania in 1853. Title insurance is unique from other types of insurance in that most types of insurance indemnify a person against a possible loss at a future date (for example, a loss in a car accident). Title insurance indemnifies the insured against losses from past events.

To lessen their risk, title insurance companies search public records to develop and document the chain of title and to detect claims against or defects in the title to insure property before it is transferred.

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Can you force your commercial tenants to operate?

By Lauren M. Reap, Esquire

As owner of a commercial shopping center, what happens if the anchor tenant closes its doors, yet continues to pay rent? Would you like to terminate that lease and replace the anchor tenant with a tenant who can bring business to your shopping center, or possibly force the tenant to operate? Both alternatives sound better then leaving a vacancy in your shopping center which deters customers from shopping there. However, your lease may not allow you to terminate that tenant or force them to operate.

Many leases include a covenant to operate, which requires a tenant to operate at the leased premises continuously throughout the lease term.

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If a lien is found, the title insurer may require the lien to be paid off, or it may create a policy exception so the lien is not insured. Title insurers take risks since there are sometimes errors not clearly reflected by the recording system. The title insurer will cover an insured party for claims arising from defects-- some examples are deeds executed by minors or mentally incompetent persons, forged instruments, corporate instruments executed without proper corporate authority and, traditionally, errors in the public record.

A recent decision from the United States District Court for the Middle District of PA found that subsequent purchasers bought a property subject to a prior mortgage despite having purchased title insurance when the title company mistakenly concluded that a prior mortgage was satisfied. *Ingomar Limited Partnership, v. Current, et al.*, 2008 U.S. Dist. LEXIS 17668 (M.D. Pa. 2008). In *Ingomar*, a couple, the Currents, executed a note and believed that the mortgage attached to the smaller of two adjacent parcels they owned. Several years later when the Currents applied for a loan to construct a house on the larger parcel, the couple found out that the lien attached to both parcels. The Currents contacted the mortgage company to remove the lien from the larger parcel. The Currents received a satisfaction piece containing addresses for both parcels but only the tax identification number of the larger parcel stating that the mortgage was satisfied and discharged. The Currents stopped making payments on the note once they received the satisfaction piece despite knowing: (1) that almost $98,000 was still owed on the note; (2) that the satisfaction piece was only to apply to the larger parcel; and (3) that the mortgage was to remain of record for the smaller parcel.

The Currents sold the smaller parcel. The new owners' title search located the mortgage lien and the satisfaction piece. The court agreed with the mortgage company's argument that the new owners were not entitled to rely on the satisfaction piece as a release of the mortgage lien on the small parcel because the release only referred to the tax identification number of the larger parcel, not the smaller one. The court found that the discrepancy between the parcels identified in the mortgage lien and the parcel referenced in the satisfaction piece placed new owners on notice of potential encumbrances to the title of the small parcel. They could not rely on the search performed by their title insurer as a basis for claiming that the mortgage should be satisfied of record.

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The court did not rule out a possible claim by the new owners against their title insurance company for its failure to discover the mortgage; that particular issue was not addressed because it was not properly before the court.

This case illustrates the need to carefully review all information regarding the title to real property. This article provides general information about title searches and the satisfaction of mortgages. Anyone with questions about mortgages, title searches and insurance is encouraged to meet with an attorney to discuss the issue.

Can you force your commercial tenants to operate? from page 1

A covenant to operate clause protects the landlord by offering him a remedy in situations where a tenant refuses to operate. A Lease without the covenant favors the tenant.

Some leases contain "use" clauses, which restrict the uses to which the leased property may be put. A clause might require that only sporting goods be sold. A "use" clause may not afford the same protections that the covenant to operate affords, because it does not require that a property be used.

A covenant to operate is an essential component of a lease if having a vacant store in the middle of a shopping center is a concern, or if a lease provides for receipt of a percentage of the business' monthly or weekly sales. So, if you have a lease without a covenant to operate, what will courts do?

Courts in Pennsylvania say that a lease lacking a covenant to operate may have an "implied" covenant to operate if the totality of the circumstances surrounding the lease support such a finding. "In construing a lease to ascertain what obligations respecting use and occupancy it imposes on the tenant, and thus in ascertaining the intentions of the parties to the lease, a court will construe the lease as a whole in light of the circumstances surrounding its execution." *Slater v. Pearle Vision Center*, 376 Pa. Super. 580, 589 (Pa. Super. 1998). The court found Pearle was obligated to operate based on the following lease requirements: that the store open to the public within 90 days from Landlord's approval of the plans; that Pearle conduct its business on the entire premises; that Pearle not abandon the premises except for approved renovations or transitions; and that Pearle operate its store in "a manner consistent with the character of the shopping mall."

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Further, the court cited a New Jersey Supreme Court decision in which the court, distinguishing the case before it from previous decisions, stated "these cases and others like them, did not involve the precise use and occupancy language in the lease before us and, much more to the point, did not involve a situation where, as here, there were interdependent economic units and the landlord had an obvious interest in the continued active operation of the leased premises far beyond the mere payment of the fixed monthly rental." *Ingannamorte v. Kings Super Markets, Inc.*, 55 N.J. 223, 227 (N.J. 1970).

Although these outcomes seem reassuring, not all states come to the same conclusion. An appellate court in Missouri recently held otherwise in *Giessow Restaurant, Inc. v. Richmond Restaurants, Inc.*, 2007 Mo. App. LEXIS 1098 (E.D. Mo. 2007), where a restaurant closed and continued to pay rent. The *Giessow* court applied strict construction and found that if the lease does not contain a covenant to operate, one would not be implied. The sub-lease in question contained a use provision and a requirement that tenant pay landlord a sales percentage in addition to the base rent. However, the court refused to find an implied covenant to operate holding that the sub-lease's use provision only restricted the use the property could be put to when the property was in use, and that the fixed rent component of the lease, $25,000.00 per year, was substantial enough so that the percentage component would not be dispositive of whether there was an implied covenant to operate.

States may be split on whether to imply a covenant to operate, but Pennsylvania courts seem to support such an implication if the totality of the lease and circumstances surrounding its execution and implementation support such a covenant. However, the best advice would be to include an explicit covenant to operate in all your commercial leases.

This article addresses a limited issue concerning commercial leases. The facts and circumstances of each situation differ and the outcome of each case may be different. Anyone with questions regarding a commercial lease should contact an appropriate professional for advice on the lease in question.

Closely-Held Business Disputes: Dealing With Conflicts Between Equal Owners

By Michael Mattioni, Esquire & Jennifer Iacono, Law Clerk

A closely-held corporation is one owned by relatively few shareholders, the majority of whom participate in the management and operation of the corporation. Often management of these corporations is informal, with little or no documentation regarding the roles of the shareholders. When things are running smoothly, this is not a problem; when disputes arise, drastic consequences may result.

When there are two equal percentage owners of a corporation, unique problems often arise. It is impossible to create an alliance of the majority of shareholders to force out or to overrule the objecting shareholder, resulting in a deadlock. What is the duty owed between equal shareholders to each other?

In a recent decision by the Court of Common Pleas in Centre County, it was held that equal owners of a closely-held corporation are each entitled to the other's performance of fiduciary duties of loyalty, good faith, and full disclosure. *Edwards v. Agostinelli*, No. 2006-3286 (C.P. Centre Oct. 16, 2007). This is a potentially significant decision, but it is not binding precedent as it is not a final decision of an appellate court. It will be interesting to see how the appellate courts handle this issue.

In *Edwards*, plaintiffs Jon and James Edwards filed claims against defendants Edward and Linda Agostinelli. Plaintiffs alleged, among other claims, that defendant Edward breached his fiduciary duty to the plaintiffs by appropriating and converting funds invested by plaintiffs into LETWO, a corporation held by all the parties, for his own benefit and the benefit of his immediate family. It was also alleged that defendant Linda breached her fiduciary duty to act in good faith by failing to stop her husband from converting the funds for his own use, and additionally, wrongfully excluding the plaintiffs from the business. Plaintiffs also filed claims against Linda for breach of her fiduciary obligation to protect the interests of the plaintiffs as minority owners, and for failure to refrain from conduct that would injure LETWO or its members. As a result of these adverse actions, plaintiffs sought damages for losses resulting from damage done to the reputation of the corporation, and other related remedies.

The *Edwards* court, in finding that the plaintiffs as equal owners were entitled to fiduciary duties of loyalty, good faith, and full disclosure from the other shareholders, and allowed the claims to move forward.

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Thus, the court determined that it would allow claims for breach of fiduciary duty to proceed, even though the shareholders were equal owners. This is significant because it is established law that a majority shareholder of a closely-held corporation owes the minority shareholders a fiduciary duty. There is no clear cut duty established between equal shareholders.

This decision highlights the need for shareholders or owners of closely-held businesses to prepare written agreements that outline their responsibilities to each other and the business. While not perfect, such agreements often go a long way in keeping disputes among owners of a business from escalating into costly and time consuming litigation.

Corporations are generally governed by certain charter documents, such as by-laws; however, these documents are often supplemented with shareholder agreements which are common among corporations with relatively few shareholders.

Shareholder agreements may, and should, include special "dispute resolution" provisions which set forth alternative ways for dealing with a dispute among shareholders. These alternate methods of dispute resolution generally include arbitration and/or mediation. Such provisions may govern situations such as that described above where one owner takes action detrimental to the company, or may also help resolve disputes where co-owners cannot agree on the operation and management of the corporation: that is "deadlocked."

By entering into a shareholder agreement, equal owners can establish what is expected of each other in terms of management of the corporation, and the remedies afforded to aggrieved shareholders. Moreover, shareholders can establish those methods by which disputes can be settled in order to prevent having to go to court.

This article provides general information concerning disputes among equal owners of a closely-held corporation. It is not intended to be a comprehensive overview of the issues. Anyone with questions regarding closely-held corporation disputes, or wishing to enter into a shareholder agreement, should contact an attorney or other appropriate professional.

Firm News and Updates

James DeMarco, Jr. joined the firm in June, 2008 in an of counsel position. James handles litigation matters in courts of the five county of Philadelphia region and beyond, concentrating on plaintiff's litigation with a focus on personal injury matters. James also has been rated as a Rising Star in Super Lawyers by Philadelphia Magazine in 2005, 2006 and 2007 in the area of general litigation… **Dawn M. Tancredi** was elected to the Board of Governors of the Justinian Society, a legal organization whose members include Italian-American lawyers, judges and law students… **Joseph Bouvier** was recently elected to the Board of Directors of the Swedesboro Woolwich Business Association, which serves to promote businesses in the Swedesboro, New Jersey area and to preserve and improve the Swedesboro downtown business district… **Stephen J. Galati** was elected Vice Chairman of the South Harrison Township, New Jersey Economic Development Committee. On May 28, 2008 Stephen was a speaker at a seminar that was titled "Trucking Litigation: Handling Various Issues Unique to Trucking in Pennsylvania." Stephen was also elected to serve as the Chairman of the International Refrigerated Transportation Association ("IRTA") for 2008-2009. IRTA is an international, non-profit organization created to cultivate, foster and develop commercial and trade relations between those engaged in all aspects of producing, importing, exporting, transporting, warehousing and otherwise dealing with commodities requiring temperature and/or atmospheric controls and related services… **Mattioni LTD.** Recently held a well-attended reception in our Swedesboro office welcoming our New Jersey clients.

MATTIONI, LTD.

COUNSELORS AT LAW

Philadelphia Office
399 Market Street
Suite 200
Philadelphia, PA 19106

Phone:
(215)-629-1600

Fax:
(215)-923-2227

E-mail:
firmmail@Mattioni.com

New Jersey Office
1316 Kings Highway
Swedesboro, NJ 08085

Phone:
(856)-241-9779

Fax:
(856)-241-9989

Montgomery County Office
509 Swede Street
Norristown, PA 19401

Phone:
(484)-322-0886

Fax:
(484)-322-0887