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Preface

The primary purpose of any instructional text is to be both easy to understand and authoritative. This is not a simple matter when discussing real estate law. When made simple to understand, concepts often become so nebulous, and so many details and exceptions are overlooked, that an "easy-to-understand" text may tend to be misleading, vague, and subject to overgeneralization. It has been my experience, in teaching the basic principles of real estate, to find licensed salespeople and brokers misconstruing a basic implication of property law because of overbroad statements they have heard or read through "easy-to-understand" instruction.

On the other hand, most people find it too frustrating and time-consuming to search through *Powell on Real Property** to understand the basics of a standard mortgage form. It has often been a criticism of attorneys that they are so detail conscious that they "can't see the forest for the trees," and that they tend to hinder a real estate transaction rather than seek to expedite the closing process.

This book is intended to make some headway in bridging the gap between these two extremes. I have attempted to cover most pertinent topics in real estate law as it exists today. An in-depth study of dower and curtesy and fee tail estates and the long history of seizin and feoffments have been minimized to narrow the broker's scope of instruction to more up-to-date applicable problems and solutions. In this same vein, the more complex areas of securities law, federal regulations, sophisticated zoning theories, and other more complicated collateral sources of law and their effect on real estate have been omitted to avoid confusion. These areas will be left to the never-ending accumulation of litigation,

* Richard R. Powell, *Powell on Real Property*, Patrick J. Rohan, Ed. (New York: Matthew Bender & Company, Inc., 1977). This constantly updated set of books is considered to be one of the most authoritative works on real property law.

legislation, and articles published for the benefit of the legal profession.

A special effort has been made, however, to utilize a certain amount of detail in those areas of real estate law that prompt the bulk of questions that occur during the day-to-day operation in the broker's office and that relate to the real estate basics that lawyers who are engaged in the business of general practice of law will encounter. Legal periodicals, statutes, and cases are used freely in an effort to facilitate the steps toward more intensive research to aid the more advanced student of the law. To aid in understanding, uniform state laws have been referred to where applicable in order to both emphasize the similarities and clarify the differences existing among the states.

Forms have been inserted for illustrative purposes only. No standard form can be used for all purposes, and competent legal counsel should be employed to draft and interpret all legal documents. To prevent monotony, there has even been an attempt to inject humor amidst some of these magnificently interesting topics.

I welcome constructive criticism of this textbook and would appreciate hearing comments.

Charles J. Jacobus

Contents

1

Introduction to the Basic Processes of Real Estate Law

THE ROLE OF REAL ESTATE LAW

Brokers and lawyers will surely agree on one thing—that the real estate business is becoming more and more complex. The common-law doctrines that have controlled real estate law for centuries are eroding away as a result of innumerable statutes, both at the federal and state level, which often seem to create more problems than they solve. However, this erosion is yielding some benefits in that it requires both brokers and lawyers to become more proficient and more sophisticated in keeping up with these areas of the law, and this could well force both brokers and lawyers to a more conscientious attitude in representing their various clients' interests. It has also drawn much more attention to the fact that real estate is a constantly changing subject and one that is rapidly becoming a field for true professionals.

The real estate laws have become so diversified that one can no longer think of real estate law as only one subject. Real estate law used to consist basically of brokerage negotiation, drawing legal instruments, and establishing and litigating various property rights. Only a few years ago, real estate law was just a small segment of every lawyer's practice. Today, real estate involves a much broader scope of law as a result of constantly changing aspects of mortgage law, new developments in usury, changing definitions of "interest," and modifications of agency theory. There have also been new developments in contract law, securities law, and land use planning law. In addition, there are frequent changes and supplements to landlord and tenant laws, mechanics' and materialmen's liens, and the probate, estate, and community property laws that are unique to each state. Then to this list one must add the never-ending anathema of federal regulations.

A good example to typify this problem of diversity is a situa-

tion that arose as a result of a marketing suggestion from a real estate agent who represented a particular builder. The agent had a good idea of marketing his client's townhouses by selling them as real estate investment "packages" to investors across the country. It was a very elaborate scheme, well done, and would have probably been very successful. However, imagine the look on this man's face, very enthusiastic about marketing this real estate (and anticipating his commission money rolling in!) when he was told that such a marketing plan, although involving sale of real estate, violated the Securities and Exchange Acts of 1933 and 1934 and was unquestionably illegal. His particular marketing plan changed the character of these real estate parcels into "securities," as defined by the Securities and Exchange Commission. Such startling discoveries are now becoming quite commonplace in a field where the interaction of various laws can further complicate the transaction of real estate agents and businessmen.

As we accept this premise, there is yet a deeper problem that is much more intrinsic to the real estate business; that is, a client often has two representatives, his real estate agent and his attorney. Now, couple this with the fact that there are at least two clients in most transactions (making a total of at least six interested parties—*all* of whom are striving to "protect" someone), and the result is that the problems, stories, and third-hand information (and misinformation) contribute mistrust and confusion to what is already the overregulated field of real estate law. This results in brokers versus lawyers, brokers versus brokers, lawyers versus lawyers, clients versus clients, and every other permutation and combination that can logically result from the proverbial "can of worms."

THE VARIOUS LAWS

It is interesting to note the various priorities of the laws and how they have come to interact with each other over their years of development. There are two basic sources of statutory law—one state, the other federal. In the area of real estate, state law has generally been considered controlling because of the peculiarities of the backgrounds and doctrines that various states have evolved over the years. However, we are finding in more recent times that the federal government is now taking a vital interest in protecting people from themselves and in passing voluminous amounts of federal legislation to regulate the real estate business.

Constitutions

Our basic sources of law are found in our state and federal constitutions. The U.S. Constitution is the primary source and vests

in all citizens of the United States certain inalienable rights that are considered inviolate and so basic to our system of government that no statute, ordinance, or any contractual right can waive the obligations or privileges therein contained. It is from this document that our individual freedoms and prohibition from abridging these individual freedoms are derived. For instance, discrimination on the grounds of race, color, or creed is considered patently unconstitutional, as is the denial of one's property rights without "due process of law." No statute, contract, or restriction upholding same will ever be enforced. Constitutional rights are, of course, the most important legal rights that one can have, and these rights can only be altered by constitutional amendment.

It must also be remembered that this same Constitution also gives the federal government extraordinary powers of enforcement when it comes to federal laws or federal issues that are considered within the parameters and scope of the Constitution. In the field of real estate, one of the more important areas comes under the interstate commerce clause. For example, Congress is finding more and more ways to regulate *intrastate* real estate activities because of the far-reaching effects these have on other states by virtue of the use of the U.S. mail, telephone, or other means of *interstate* commerce. This will be discussed in greater detail in a later chapter.

Each state also has a constitution, and in this constitution are certain inalienable rights that apply to the citizens of that state. These rights basically come from the codification and derivation of the heritage of the state and embrace a myriad of subjects, including the homestead laws, certain mechanics' and materialmen's lien laws, and the community property rights or other marital property rights that may exist. One must remember that when these rights are constitutional, they cannot be waived by private contract or by subsequent statute or ordinance. The individual rights embraced by the state constitution are usually far-reaching and in much greater detail than those of the U.S. Constitution. However, if there is a conflict between the U.S. Constitution and the state constitution, one can generally consider that the U.S. Constitution would control if the issues involve a federal issue (i.e., an issue over which power has been delegated to the federal government by the Constitution) rather than a substantive state question. If the issues involved are purely state issues and do not involve powers granted to the federal government or rights reserved to individuals, the U.S. Constitution would not be involved because of the Tenth Amendment, which reserves all powers not so granted to the states respectively. If the

courts determine that a federal issue exists, the U.S. Constitution would control over the state constitution.

Statutes

The sources of law that affect property rights in greater detail (than what is favored in the federal or state constitutions) are those created by our legislatures, both state and federal, in their infinite wisdom. Of course, a law or a statute can be declared unconstitutional and its enforcement prohibited, which, of course was what happened to laws on racial discrimination in the South for many years. The conflict between statutes and constitutions is often a very technical and complicated legal problem and need not be delved into at this point. However, it is clearly understood that all statutes have the force of law until declared unconstitutional by the courts. In case of a conflict between federal and state laws, federal law would control if there was a federal question involved. However, as in constitutional matters, if the issue is a particularly unique state matter of substantive law, the state statute would control, the theory being that under the Tenth Amendment to the U.S. Constitution and the derivation of local laws, the local statute is probably more pertinent to conditions as they exist in that state. In more current times, however, federal statutes seem to be getting more favoritism because of the more liberal interpretation of the federal powers given by the courts.

Ordinances and Regulations

Beyond the statutes at the state level, we generally encounter the various categories of municipal and county ordinances, as well as the rulings and regulations of the various state agencies. Those decisions made by state agencies that have quasi-judicial power (the agency can make binding decisions pursuant to the scope and powers under which that agency was created) are generally considered to have the force of law unless there is a clear abuse of discretion on the part of that particular state agency. City and county ordinances must, of course, undergo the same constitutional scrutiny that state statutes are subject to. The local ordinances are inferior to state statutes when there is a conflict in the two laws.

Beyond the statutes at the federal or state level, one encounters the far more extensive rulings and regulations of state and federal agencies. The large number of regulations are a result of the fact that the various laws are often very broad, often vague,

and always confusing. The particular agency whose duty it is to enforce the law, therefore, passes its own regulations that serve as guidelines on how that agency is going to interpret and enforce the law passed by the legislature. These regulations can be changed at the whim of the regulatory agency. For instance, the Internal Revenue Service can change its position on particular tax exemptions or how it will interpret a certain portion of the Internal Revenue Code. This same type of change in position can occur in all agencies, and each agency regularly publishes rules and regulations that can even expand that agency's scope of jurisdiction; a rule or regulation can be issued to clarify a stand that the agency may have taken previously, even though the effect on the taxpayer may be entirely different. These rules and regulations issued by the agencies have, of course, the effect of law, subject to review by the courts. It is in this area that the federal government is gaining more and more power, which may or may not have been the purpose of the original Congressional acts enacting the legislation.

Judicial Interpretation

Too often the interplay of people's emotions and interpretations of laws results in decisions being made by the final arbiter, the court system. Although sometimes unpredictable, this system is probably the best in the world. It is the basis from which precedents are set and priorities are maintained, and the courts often expose additional questions and interpretations that then become the foundation for new laws and statutes.

HISTORICAL BACKGROUND OF THE COURTS

Courts of Law

Our present court system arose from a centuries-old system of an objective third party making a fair and just decision to solve a problem between two adversaries. As our structure of the law developed through basic legal principles and doctrines of equity, the written aspects of a transaction were carefully and rigorously adhered to, as being important for an orderly society. Since the principles of law were fairly well settled back in the seventeeth century, when one might consider disorder as being a little more commonplace, this rigorous interpretation of law was probably a logical approach to setting up a civilized and ordered society. As a result, we fell into the situation where, if a man breached his agreement by being a day late for his mortgage payment, the

mortgagee thereunder could foreclose, having the agreement strictly upheld in the courts of law. The mortgagor (who is generally the purchaser), then, could lose his property because he was a day late in making his mortgage payment, or for some other minor breach of the contract between the parties, even though the circumstances surrounding this breach may have been beyond his control.

Courts of Equity

As our system of justice evolved, however, courts of equity were established to soften the impact of these strict legal principles. These equity courts had particular significance in the area of real estate, since real estate is considered unique and money damages could not compensate for its loss. The equity courts had concurrent jurisdiction with the courts of law, which were still in existence, and would impose their jurisdiction when fairness or equity dictated that the rules in some circumstances were too strict, sometimes changing the result. For instance, if a farmer could not make his mortgage payment on the day it was due because of matters beyond his control, the court of equity could impose its jurisdiction to do what was fair and would allow him to make his payment a day late, a month late, or whatever was "reasonable" to see that equity and justice were done.

The courts of equity also imposed precedent by establishing certain equitable principles. These principles, such as "unjust enrichment," "unconscionability," and "irreparable harm," were used as reasons to find an equitable conclusion. They were created and construed ad infinitum (or ad nauseum, depending on your point of view) and resulted in literally hundreds of clichés, often called *equitable maxims,* which were ultimately used as precedents to control later decisions. Although having no true legal effect, these maxims could always be used as grounds for the defendant and were easy to roll off the lips, so that silver-tongued orators could constantly remind the court that "he who seeks equity must do equity"; "equity does that which ought to be done"; and the all-time favorite, "he who seeks equity must have clean hands."

It was in these courts that equitable remedies such as specific performance, rescission and restitution, quantum meruit, and quasi-contractual recovery (to name a few) were imposed. These remedies, of course, differ from damages and actions in tort or contract, which arise under the law (and for which the damaged party can get money damages or recovery of his property). *Specific performance,* for instance, is generally granted where damages are

not shown to be adequate and just remedy and can only be enforced when there is not an adequate remedy at law. *Rescission and restitution* generally arise when the breach of the contract constitutes a failure of the consideration bargained for and the nonbreaching party prefers to rescind the contract and sue for complete restitution of whatever benefits have accrued to date. *Recission* is the voiding of the contract or agreement. *Restitution* is the restoration of the parties' original rights. In this particular equitable remedy, the parties are put back in the same condition that they were in prior to execution of the contract. *Quasi-contractual* principles generally arise when there has been something material omitted in the original contract and the court imposes its own contractual principles as if these had been bargained for and written in the contract itself. This is also the principle behind *quantum meruit*, where one party performs his part of the obligation and the breaching party refuses to pay (or perform). In this situation, the court can impose quasi-contractual remedies in order that the party performing the duties be paid the reasonable value of the performance rendered.

It is interesting to note that these remedies, which are not by any means all of the equitable remedies available, are not conferred by statute or by any other type of codified jurisprudential consideration. They are remedies that have evolved over the years through the courts seeking fair and just results, and are particularly applicable to real estate. Real estate has always been considered to be unique and valuable. Courts have therefore tended to use these equitable principles to prohibit loss of title, foreclosures, or restrictions on use when there is only a minor breach of obligations.

THE CURRENT CIVIL COURTS SYSTEM

The court systems, as they exist today, have both legal and equitable jurisdiction merged into the same court. The distinction between the different state courts, although their legal and equitable jurisdictions are similar, is not always simple. The jurisdictions of these courts are statutory and are maintained separate and distinct for the purposes of expediting the judicial process and facilitating access to the court system. To help simplify this explanation, we will discuss only the civil (and not the criminal) court systems. These civil court systems, for the purposes of this discussion, will be divided into two distinct and separate systems. The first is the state court system, which, in order of ascending importance, includes the small claims, trial courts, courts of civil appeals, and the state supreme court. The second system is the federal system,