

## Real Estate Cases To Watch In 2015: Midyear Update

By **Natalie Rodriguez**

*Law360, New York (June 30, 2015, 4:34 PM ET)* -- From proposed class actions challenging energy pipeline rent deals with railroad companies to rumblings of disputes emerging from the market's construction boom, real estate experts have their eyes on several new fronts of litigation in the second half of the year.

The Supreme Court on June 25 packed away one of the top cases property lawyers had been watching when it ruled on disparate impact, but several other high-profile suits continue to unfurl, and there is important new litigation bubbling up over issues from railroad rents to fracking bans, so there's plenty for real estate lawyers to be keeping their eyes on.

Here are a few of the new cases and trends to watch in the latter half of 2015.

### **A Pipeline of Proposed Class Actions Over Rail Rent**

In the last two months, Union Pacific Railroad Co. and Kinder Morgan Inc. have been hit with a pair of federal lawsuits alleging that Union Pacific didn't own the pipeline easement rights given to Kinder Morgan and that the railroad illegally collected rent. The suits could be just the start of a watershed of litigation that may hit railroad and energy companies in the coming months and years, according to Brandee Caswell, Faegre Baker Daniels LLP's real estate litigation practice leader.

"This would apply to every railroad out there and this is a very slippery slope," Caswell said.

The first suit was filed in May in Arizona by a proposed class led by Robert D. Clements and Robert D. Zimmerman, who claim Union Pacific unlawfully utilized landowners' subsurface rights in the 1950s to construct an underground petroleum pipeline within the railroad's right-of-way, despite only holding a surface easement for its railroad. The proposed class aims to represent the owners of hundreds or thousands of parcels along the right-of-way and pipeline.

Closely following was a June putative class action filed in California by Richard Bagdasarian Inc., which claimed that Union Pacific and Kinder Morgan owe landowners along a stretch of rail at least \$100 million in pipeline rent.

The suits are sparking up now, in part, because of recent court rulings that have found landowners with properties abutting rail tracks hold the underlying fee interests in the land below the tracks, rather than the railroad companies that only have easements for specific rail work, Caswell said.

If these cases see any success, they are likely to spur similar suits across the country, Caswell noted. “If you're another railroad company that hasn't been named to one of these, you're doing some due diligence ... about what the potential liability might be,” she said.

The suits are *Clements et al. v. Union Pacific Railroad Company et al.*, case number 4:15-cv-00191, in the U.S. District Court for the District of Arizona and *Richard Bagdasarian Inc. v. SFPP LP et al.*, case number 8:15-cv-00986, in the U.S. District Court for the Central District of California.

### **Construction and Lease Litigation Is Bubbling Up**

The real estate market is currently seeing a frenzy of construction in several major cities, and there is a lot of prelitigation activity occurring over alleged deficiencies with new build outs or projects — at least some of which are likely to eventually make their way into court, according to Charles D. Jarrell, a Los Angeles litigation partner with Allen Matkins LLP.

“What we're seeing more of in the past six months or so are disputes arising out of construction in tenant office space,” Jarrell said, adding that there are also increasing numbers of disputes arising from lease deals. “Tenants are fighting over option rights, renewal rights and terms.”

Generally, existing tenants are fighting to enact terms that were negotiated during a softer market, while landlords are toughening up and trying to deny expansion options or renewal rights so that new deals can be struck at better terms in this healthier market, said Jarrell, who spoke from his experience with the California markets, but noted that the area is emblematic of other cities seeing development booms.

The robustness of the office and lease deals sector is also in large part why most attorneys are trying to keep the disputes out of court, requesting litigators like himself to do confidential reviews of disputes so that projects aren't derailed off their timelines by a visit to court or formal arbitration. “That's a product of the heat of the market,” noted Jarrell. “But they're not going to be able to resolve all of those, and some will go to litigation. I imagine ... some of that is going to bubble up in a year.”

### **Fannie, Freddie Shareholder Challenge Moves Forward**

As noted in the beginning of the year, eyes have been on hedge fund Fairholme Capital Management LLC's challenge to the government's directing all the profits from Fannie Mae and Freddie Mac toward the U.S. Department of the Treasury. The company alleges the government acted unconstitutionally when it altered its bailout deal for the government-sponsored enterprises to keep the companies' profits for itself.

The parties are currently deep into discovery, and a spat has recently arisen over the plaintiff's attempt to remove a “protected” designation from the depositions of former Federal Housing Finance Agency Acting Director Edward DeMarco and interim FHFA ombudsman Mario Ugoletti. A status conference on that motion has been tentatively penciled in for July, according to court documents.

The case is *Fairholme Funds Inc. v. U.S.*, case number 1:13-cv-00465, in the U.S. Court of Federal Claims.

## **A New York Suit Could Change Lease Contracts**

A spat over a broken office-lease deal in Staten Island could have significant ramifications for commercial lease deals throughout the state and elsewhere. In the case, lower courts had found that Globe Alumni Student Assistance Association Inc. was on the hook for \$1.48 million after breaking its lease months after inking a nine-year extension, which the landlord sought to immediately recover under an accelerated provision in the agreement.

But the state's high court in December remanded the case to find whether the acceleration was grossly disproportionate to the landlord's losses.

“There is a fine line between permissible damages and unenforceable penalties. If not properly drafted, acceleration clauses may be unenforceable,” said Dan Ansell, Greenberg Traurig LLP's real estate litigation co-chair. “This case is of interest because it could impact the way leases are drafted not only in New York, but also across the country.”

The suit is 172 Van Duzer Realty Corp. v. Globe Alumni Student Assistance Association Inc., case number 113137/09, filed in the Supreme Court of the State of New York, Appellate Division, First Department.

## **Broker Labor Suits May Change How CRE Deals Operate**

There is a pair of employment suits working their ways through the court systems in Massachusetts and California that question whether real estate salespeople — who must work under the supervision of a real estate broker — can be rightly considered independent contractors. With both cases, the salespeople contend they have been misclassified and should be considered full employees with benefits since they are not in control of their work.

“These cases could significantly change the interaction between real estate brokerage companies and their salespersons,” Ansell said.

In early June, Massachusetts' top court affirmed a decision to toss the suit, but plaintiff's counsel told Law360 at the time that they were considering possible next steps. The California case, meanwhile, has been slowly moving toward trial.

The suits are Nesto Monell v. Boston Pads LLC, case number SJ-11661, in the Massachusetts Supreme Judicial Court and Ali Bararsani v. Coldwell Banker, case number BC495767, in the Superior Court of the State of California, County of Los Angeles.

## **Fracking Bans Take Local Land-Use Issues to Federal Court**

Earlier this year, New Mexico became the first state to have its federal court address local ordinances banning hydraulic fracturing on properties, but it likely won't be the last that will have to address the issue, according to Caswell.

In Caswell's home state of Colorado, for one, the governor has negotiated a stand-down with energy companies by promising a legislative fix to issues. “We've got our cases on ice, but if that legislative fix doesn't happen, we're going to see [those cases move forward],” Caswell said. And the New Mexico decision — SWEPI LP v. Mora County — invalidated the local ordinance after the court found the law violated the U.S. Constitution's supremacy clause and the state's law governing oil and gas drilling.

“Land use is usually a local concern,” Caswell noted. But with the fracking bans, he said, it will become a state issue once the courts begin weighing in.

--Additional reporting by Aaron Vehling, John Kennedy and Jacob Batchelor. Editing by Mark Lebetkin.

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