Mascoma Sav. Bank, FSB v. Niteen Hotels (VT) LLC, No. 71-2-08 Wrcv (Eaton, J., Feb. 26, 2009)

STATE OF VERMONT
WINDSOR COUNTY

MASCOMA SAVINGS BANK, FSB	)	
	)	**Windsor Superior Court**
v.	)	**Docket No. 71-2-08 Wrcv**
	)	
NITEEN HOTELS (VT) LLC,	)	
VALLEY LAND CORPORATION,	)	
et al.	)	

DECISION
Plaintiff's Motion for Summary Judgment, filed Sep. 30, 2008
Valley Land's Motion for Partial Summary Judgment, filed Oct. 31, 2008

This case involves the disposition of a dilapidated hotel in White River Junction. The present matters before the court are two motions for summary judgment seeking rulings on the post-foreclosure applicability of several provisions contained in the hotel's commercial lease agreements.

The following undisputed material facts are helpful to an understanding of the case. In 1971, predecessors to defendant Valley Land Corporation leased raw land to the White River Corporation for the purpose of building and operating a hotel and restaurant. The lease required the lessee to take responsibility for building and operating the hotel and restaurant. The lease also provided for the right of the landlord to re-enter the property and take fee simple title to all buildings and improvements either at the end of the lease or in the event of a lease default.

The hotel was constructed and operated according to the terms of the lease for several decades. There were several lease amendments during that period. Among those lease amendments were provisions clarifying that the lessee is the title owner of the buildings and improvements so long as the lease remains in full force and effect.

In 1998, the lessee (White River Corporation) transferred its leasehold interest to defendant Niteen Hotels, who purchased the interest using a loan from Mascoma Savings Bank. The loan was secured by a mortgage on the leasehold interest and the buildings and improvements. In connection with this transaction, the lender, lessee, and landlord executed a number of documents clarifying the respective rights and obligations of the parties. The hotel operated under this arrangement until late 2007.

In late 2007, Niteen Hotels fell behind on its rent payments to the landlord. Pursuant to the terms of the 1998 agreements, the landlord offered Mascoma the opportunity to cure the defaults by paying back rent. Mascoma accepted the opportunity and cured the defaults. Mascoma continues to pay rent at present, and the landlord is accepting the rent payments.

In addition, the hotel was closed in late 2007 for two separate reasons. The first was that the Vermont Department of Health ordered closure of part of the hotel for problems associated with mold. The second was that the Town of Hartford ordered closure of the remainder of the hotel because of structural problems with the roof. Since then, the rest of the hotel has fallen into bad order and repair. The landlord has advised Mascoma that each of these conditions constitutes waste in violation of the lease, and that the defaults cannot be cured unless the mold problem is eradicated, the roof is repaired, and the remainder of the premises are put into good working order. These defaults have not been cured at present.

In February 2008, Mascoma commenced foreclosure proceedings against Niteen Hotels' leasehold interest. In response to the complaint, the landlord filed counterclaims seeking declaratory rulings regarding (1) whether it may terminate the lease and dispossess the lessee pursuant to its right to re-enter the property and take fee simple title to all buildings and improvements in the event of default, (2) whether the bank retains the power to exercise the lessee's option to buy the underlying property, and (3) whether the bank must keep insurance on the property. The parties subsequently agreed that these questions should be severed from the foreclosure proceedings and addressed separately, after judgment of foreclosure had been entered.

Mascoma has since obtained a judgment of foreclosure and purchased the buildings and improvements at the public sale. The foreclosure sale is presently awaiting confirmation.

The parties have now asked the court to rule upon the issues presented by the counterclaims. They have filed separate motions for summary judgment on the questions of whether the landlord may terminate the lease and whether the bank retains the power to exercise the option to buy the property. The court addresses these issues with the following rulings.

Whether the lease is currently in full force and effect

The first question presented is whether the lease is currently in full force and effect, or whether the landlord may presently terminate the lease based on the defaults related to waste. It is undisputed that the hotel has gone to waste, that this constitutes a violation of the lease terms, and that the landlord has notified Mascoma of this default.

There are two agreements between the parties that control. The first is a provision in a 1986 document known as the "third lease amendment." It provides generally that the lender must be afforded an opportunity to cure any default on the part of the lessee, and that the "time during which such default may be cured shall be extended for such period as may be necessary" to complete the cure under the following conditions: (1) the default cannot be cured by the payment of money, (2) the default cannot be cured within a 30-day period because of the nature

of the default or because the lender requires time to obtain possession of the premises, and (3) the lender pursues the cure with reasonable diligence and continuity.

The second agreement is a provision in a 1998 document known as the "landlord's estoppel certificate." This is an agreement that was made between Valley Land, Niteen Hotels, and Mascoma Savings Bank. It also provides generally that the lender must be afforded an opportunity to cure any default on the part of the lessee. In addition, it specifies that the landlord will not terminate the lease if the lender cures the default within 30 days of notice or if the lender commences timely action to cure the default when (1) the default cannot with diligence be cured within 30 days and (2) the lender pursues the cure with diligence.

The landlord has now conceded that the above provisions apply. In particular, the landlord has conceded that the lender needed time to obtain possession of the premises in order to begin the cure, and that the lender has not yet obtained possession because the sale has not yet been confirmed and the extended redemption periods have not yet ended. In addition, the landlord has conceded that the lender will not be able to cure the waste within a thirty-day time period after it takes possession.

The court would have reached these conclusions even if the concessions had not been made. Thus, the court rules that the lease is currently in full force and effect. The time during which the default may be cured will begin when Mascoma takes possession of the property, and shall be extended for such period as may be necessary so long as the lender pursues the cure with reasonable diligence and continuity.

Whether the landlord has waived its reversionary interest

Mascoma has argued that the landlord has waived its right to terminate the lease and take possession of the buildings and improvements by accepting rent after the time period for curing the default related to waste had expired. *Andrus v. Dunbar*, 2005 VT 48, ¶ 12, 178 Vt. 554. Given the foregoing ruling that the time within which the default may be cured has neither started nor expired, the waiver rule stated by *Andrus* does not apply to the facts of this case. The landlord has not waived its interests by accepting rent.

Mascoma also argues that the landlord waived its right to take fee simple title to the buildings and improvements through various lease amendments that have been made during the years. However, the referenced lease amendments merely clarified that the buildings and improvements on the property were owned by the lessee "so long as this Lease remains in full force and effect." The court interprets these amendments as defining the state of title to the buildings and improvements during the life of the lease, and not as modifying the relationships of the parties upon termination of the lease by expiration or default. There is nothing in the amendments that shows an unequivocal intent on the part of the landlord to waive its reversionary interests, or that equitably prevents the landlord from asserting its reversionary interest at a later time. Cf. *Anderson v. Cooperative Ins. Co.*, 2006 VT 1, ¶ 11, 179 Vt. 288 (explaining that waivers must be express or unequivocal); *Fisher v. Poole*, 142 Vt. 162, 168 (1982) (explaining that party asserting equitable estoppel must show that its reliance on a representation was reasonable).

Finally, Mascoma argues that the reversionary interest was lost in the foreclosure judgment. The court does not agree because the foreclosure judgment specifically provided that issues raised in the counterclaim (including the right of the landlord to terminate the lease and take possession of the buildings and improvements) were severed from the judgment. In addition, the foreclosure judgment covered only the leasehold interest. It did not purport to amend the terms of the lease to the benefit of the lessee.

Whether the bank may reassign the lease

The parties have asked the court to declare whether the lender may reassign the lease after taking possession. Without addressing the subtext of this question, which is discussed in more detail below, the court briefly answers this question in the affirmative. The 1998 landlord's certificate provided that in the event of a default by the borrower, the lender "may reassign the lease," and the landlord's "consent to any such reassignment will not be unreasonably withheld or delayed."

Whether the default may be cured by construction of a new hotel

The fundamental question presented is whether the defaults related to waste may be cured by (1) reassigning the lease to a new lessee and (2) demolishing the existing buildings and improvements and building a new hotel and restaurant.

According to the notices of default provided by the landlord, the current defaults on the hotel property cannot be cured unless the mold problem is eradicated, the structural problems with the roof are addressed, and the entire premises are put back into good working order. In its statement of undisputed material facts, Mascoma has asserted that it has investigated the possibility of restoring and repairing the hotel so that it complies with all applicable ordinances, and determined that doing so would be cost prohibitive. Mascoma therefore asserts that it would be "more cost effective in the long run to reassign the lease to a new lessee who would demolish the dilapidated building currently on the premises and build an appropriate building which complies with the applicable ordinances and lease provisions." These assertions are supported by the affidavit of bank officer Terry Martin.

The landlord argues that the assertions are conclusory, and that it has not had an opportunity for discovery as to the extent of the investigations undertaken by Mascoma regarding the possibility of restoration and the possibility of reassignment. For the following reasons, however, the court does not perceive additional evidence as being necessary to the disposition of the motion.

The foremost reason is that the lease agreements do not require the lender to undertake any specific course of action when attempting to cure a lease default. Instead, the agreements say only that the lender may attempt to cure any lease default, and that when the default cannot be cured within a specified time, the lender must pursue the cure with "reasonable diligence and continuity." This does not require the lender to follow any specific course of action when attempting to cure, so long as the cure is pursued diligently and in good faith.

In other words, it is the responsibility of the lender to select the means of curing. This makes sense because it would be unfair and economically inefficient to permit the landlord to define both the default and the means of curing, and then require the lender to follow those means even when doing so would be cost prohibitive and when other commercially reasonable means of curing were available. The court will not construe the lease agreements in a manner that requires untenable or unreasonable results. See *State v. Great Northeast Productions, Inc.*, 2008 VT 13, ¶ 10 (explaining that courts avoid construing contracts in a manner that leads to unreasonable results).

In this case, for example, it does not make sense to require the bank to sink money into the repair of a dilapidated building or to demolish the buildings itself and construct a new hotel and restaurant. The leases do not require those particular approaches, and they are not the only solutions to the problems presented by the waste currently occurring on the property. There is no reason why the bank should be forced into the role of general contractor or hotelier when it believes that the more cost effective approach would be to reassign the lease to a new lessee who will undertake demolishment and construction. The lender has every incentive to cure in a commercially reasonable and diligent manner because it is paying monthly rent to the landlord.

The landlord contends that this interpretation leaves them without a functioning hotel and restaurant as required by the terms of the lease. The court agrees that the purpose of the lease is to have an operating hotel and restaurant on the leased premises, but it cannot be overlooked that the hotel has already been shut down. The lender is not proposing to shutter a going concern. Instead, the lender is proposing to cure the waste by getting a hotel up and running that complies with all applicable ordinances. The applicable lease provisions allow the lender reasonable time within which to pursue this cure with diligence without specifying how the cure must be accomplished. For these reasons, the court rules that the lender may reassign the lease to a new lessee who may construct new buildings and improvements on the premises,[1] so long as the cure is pursued with reasonable diligence and continuity.

Whether the bank may exercise the option to purchase

In its motion for partial summary judgment, the landlord seeks a ruling that the bank does not have the power to exercise the lessee's option to purchase the property in light of the defaults related to waste.

The lessee's option to purchase the property was created in the original 1971 lease, which provided that the lessee shall have the "exclusive and irrevocable option" to purchase the property at a specified time if the lessee made all rental payments and performed all covenants and conditions of the lease for the first ten years. The sale price was to be determined by agreement between lessee and lessor, but if no agreement was reached, the sale price was to be set by a panel of appraisers selected by the parties.

[1] In the interest of clarity, according to the original lease, the landlord's reversionary interest exists in whatever buildings are "then existing" on the property upon termination or expiration of the lease. This includes any new or replacement buildings constructed during the life of the lease.

The option has expired under the terms of the original lease. However, in the 1986 lease amendment, the lessor agreed that the option to purchase "may be exercised at any time hereafter" by the lessee upon written notice, without any reference to conditions precedent. In addition, the 1998 estoppel certificate specified that the lessee "has . . . an option to purchase the Property" without mentioning any conditions precedent.

The court therefore concludes that the lessee's option to purchase the property became vested in the 1986 lease amendment, and was not subject to any conditions precedent in 2007. It was not extinguished by the failures to pay rent or the waste occurring on the property.

The court does not view this interpretation as unreasonably permitting the bank to exercise the option at a lower price than if the buildings had not gone to waste. There is no indication that the waste occurring on the property has somehow been permitted to linger in bad faith for the purpose of affecting the property's purchase price, and the parties must have contemplated at the time of the 1986 and 1998 agreements that property values would fluctuate over time. Furthermore, the original lease agreement contemplates the involvement of both parties in setting the purchase price. The court finds no reason to conclude that the option to purchase has been extinguished.

Conclusion

For the foregoing reasons, the court concludes that (1) the lease is in full force and effect, (2) the landlord's reversionary interest has not been waived, (3) the lender may reassign the lease, (4) the default may be cured by reassignment and reconstruction of the buildings so long as such cure is pursued with reasonable diligence and continuity, and (5) the lessee's option to purchase has not been extinguished. As it appears to the court that these rulings resolve the issues presented by the counterclaims, Plaintiff's attorney shall submit a form of judgment within 10 days. Any objections shall be filed within 10 days thereafter.

ORDER

(1) Plaintiff's Motion for Summary Judgment (MPR #5) is ***granted in part***;

(2) Defendant Valley Land Corporation's Motion for Partial Summary Judgment (MPR #6) is ***denied***; and

(3) Plaintiff's attorney shall submit a form of judgment within 10 days. Any objections shall be filed within 10 days thereafter.

Dated at Woodstock, Vermont this ____ day of _____, 2009.

_____
Hon. Harold E. Eaton, Jr.

Presiding Judge