Construction Law Newsletter

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MESSAGE FROM THE CHAIR

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As the construction industry retrenches and adjusts to the new realities of our economy, attorneys practicing construction law are responding. We are assisting our clients to be better prepared for a complex and competitive economic environment. Most of us have seen reductions in contract negotiations and increases in construction lien and bond claims and other construction litigation. And the economists' prognosis, as we hear it, is not cheerful. In times like these, we need to ensure that we are competent and able to guide clients toward certainty in their legal environment, protection of their companies, and efficiency in responding to opportunities.

The Construction Law Section continues to be committed to promote a collegial and knowledgeable bar in the realm of construction law, to educate attorneys about the news and nuances of this practice, and to improve the law to provide more certainty and security for our clients. Our executive committee is expanded and diverse in our practice areas (please see listing at the end of this newsletter), and is committed to improvement of the Section's members in at least the following areas:

1. Education. This newsletter has been the best source for thoughtful, Oregon-specific, and practical advice and education of the Oregon construction bar for many, many years. You can find topical and useful articles in this edition, as well as in past editions, which are available on our Section Web site: www.osbarconstruction.com. We are blessed with the continuing leadership of former chair Alan Mitchell as editor of the newsletter. Please contribute your experiences and scholarship for the benefit of all Section members. We will publish three editions this year.

Further, the Section is planning several continuing legal education programs this year and into 2011 for the specific education of construction lawyers. These will include a daylong program for both new and experienced practitioners in the central Willamette Valley sometime this fall, continuation of the "brown bag" series for newer construction lawyers in Portland, and our biennial program with the staff of the Oregon Construction Contractors Board in conjunction with our annual meeting this December. Other CLE programs are also in the works. We will be contacting you about those opportunities.

2. Improving the Law. The board has determined that, given legislative efforts in recent years to address Oregonians' concerns about the construction industry, we should attempt to improve certain statutes on a neutral, nonpartisan basis to achieve consistency and certainty in how these statutes are applied. For these matters to be considered in the 2011 Legislative Assembly, we must act before April 1, 2010, with leaders in the Oregon State Bar to set our agenda. Please contact me or any other executive committee member with your thoughts, but do it now!

At this point, we plan to submit proposals to make appropriate corrective amendments to the

Oregon Private Prompt Payment Act, the Construction Lien Law, the Residential Defect Notice statute, some miscellaneous sections of ORS chapter 701, and possibly the new statute governing filing fees in circuit courts to address specific issues, inconsistencies, or lack of definitions and parameters in these acts. Again, we are not to advocate amendments from a partisan or positional standpoint, and we must ensure that all voices in the construction bar are heard as we move forward. At a time when consistency and certainty in the law is needed, however, this is the time to improve the laws that we interpret and apply.

The Section stands on a firm footing, built by strong executive committee members, officers, and chairs in past years. We all are grateful to immediate past chair Angela Otto and her predecessors, who have done a remarkable work in the Section's efforts to build collegiality and strength in the construction bar. This year we add several new attorneys to the executive committee to expand the breadth and reach of the Section to all sectors of the practice in Oregon. We will continue to provide programs, Internet resources, and outreach to Section members around the state.

Despite perilous times in the industry, this is a wonderful time to strengthen the construction bar's response. We welcome your voice, your time, and your talents in 2010.

COMMENT: WHITHER PRIVITY IN OREGON

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As practitioners we all presumably agree that over the last few decades contractual privity has declined in relative importance as a determinative factor in the analysis of what should constitute allowable claims or recoverable damages arising from construction activities. Whatever their role in the construction marketplace and wherever on the spectrum their views may fall, anyone paying even casual attention to the national and local currents of appellate thought has observed as least some erosion of what earlier were considered meaningful legal distinctions between contract and tort principles.

Given the judicial flux, contractors, owners, design professionals, and insurers are now each subject to varying levels of uncertainty when analyzing, allocating, and pricing business risks, where the contractual and relational framework of today's construction project, (sometimes carefully-crafted, other times not), is increasingly likely to be subject to judicial second-guessing when adjudicated some years down the road. For example, ten years ago practitioners might not have given much drafting thought to the idea that one party to a construction contract could successfully pursue a negligence, as opposed to a contract, claim against the other party for damage due to defective work. Now, though, that tort risk exists, such as when a building code section provides a governing standard. *See, Abraham v. T. Henry Constr., Inc.*, 230 Or App 564, 573, 217 P3d 212 (2009)(plaintiff homeowners could pursue a direct negligence claim against their contractor for water intrusion-related damages notwithstanding contractual privity because the duty allegedly breached arose from the Oregon Building Code, an applicable standard independent of the contract).

This Comment is neither intended to provide a general survey of current Oregon case law involving contractual privity in the construction context nor to draw together the multiple threads of analysis. Instead, it considers the most recent appellate decision, a case which discards contract privity in what, for Oregon, is an entirely new way, **allowing a defendant to raise comparative fault as an affirmative defense to an express warranty claim.** *Taylor v Ramsay-Gerding Construction Co.*, 233 Or App 272, __ P.3d __ (2010), on remand from the Oregon Supreme Court, *Taylor v. Ramsay-Gerding Construction Co.*, 345 Or 403, 196 P3d 532 (2008).

Most of the decisional movement away from privity-based concepts has been in the context of relaxing limitations on affirmative claims, such as carving *Abraham*-like exceptions into the economic loss rule. However, in *Taylor* the Court of Appeals decided the trial court did not err in submitting to the jury a stucco system manufacturer's "alternate causation/comparative fault" affirmative defense to the plaintiffs' claims for construction defect damages alleging breach of express oral and written warranties. The trial court gave comparative fault instructions and special verdict forms, and reduced the plaintiffs' damage award by the percentage of "negligence" the jury attributed to the plaintiffs.

Literal reading of *Taylor* might permit other defendants in direct privity to transform the wider "proximate causation" approach to contract damages into a more narrow and less certain tort-based "solely caused" comparative fault analysis. Even if confined in application to other scenarios sharing its factual and procedural posture, *Taylor* is another result that a short time ago most practitioners would not have considered possible, let alone glassed on the legal horizon.

Taylor is the third in a series of appellate decisions in the same lawsuit, and to distinguish the most recent decision from its two predecessors it will be referred to as "*Taylor* III". The previous decisions, *Taylor* I and *Taylor* II, are found at 215 Or App 670, 172 P.3d 251 (2007), and 345 Or 403, 196 P.3d 532 (2008), respectively. Both *Taylor* I and *Taylor* II turned on the issue of apparent authority of the manufacturer's sales representative to give the oral and written warranties at issue, and are thus instructive primarily in clarifying the parties, facts, claims and procedural posture to help understand what the court in *Taylor* III is telling us about the interplay between privity-based affirmative claims and tort-based defense concepts and possible implications going forward.

The *Taylor* III Factual and Procedural Posture

The essential facts in the *Taylor* cases, as relevant to the discussion here, are relatively straightforward. The overall dispute involves the plaintiff owners' claims for damages to their hotel resulting from construction defects, and the resulting third-party claims and cross-claims for indemnity and contribution. Plaintiffs included the Taylors, the hotel owners, who asserted breach of contract and warranty claims against their prime contractor, Ramsay-Gerding and who also asserted direct oral and written warranty claims against ChemRex, the manufacturer and supplier of the exterior stucco system installed by one of Ramsay-Gerding's subcontractors. Plaintiffs' direct claims against ChemRex were based on oral and written warranties allegedly given by ChemRex's sales agent for the territory.

The relevant procedural posture was not overly complex. ChemRex asserted an affirmative defense of comparative fault in response to the direct warranty claims by the plaintiffs Taylor. Ramsay-Gerding asserted an affirmative defense alleging the plaintiffs Taylor were negligent in selecting the stucco system. Ramsay-Gerding also filed third-party claims against Ramsay-Gerding's subcontractors (and others), and cross-claims against ChemRex.

The trial court bifurcated the warranty/stucco system defect issues for trial separate from the other claims and issues. At conclusion of the warranty/stucco system trial, the trial judge instructed the jury (over plaintiffs' objection) as to ChemRex's comparative fault defense, and submitted three special verdict forms. On the first of the special verdict forms the jury found ChemRex had breached one or more of its express warranties to plaintiffs and caused them $775,000 damages, that the Taylors were negligent in one or more ways alleged by ChemRex, and that ChemRex was 51% at fault and plaintiffs Taylor 49% at fault. The second special verdict form is not relevant to this discussion. On the third special verdict form, the jury found ChemRex had breached one or more of its express warranties to Ramsay-Gerding, that Ramsay-Gerding was negligent in one or more ways alleged by ChemRex, and also found Ramsay-

Gerding 35% at fault, Chemrex 35% at fault, and plaintiffs Taylor 30% at fault.

The trial court entered judgment based on the first special verdict form, not the third, thus entering judgment for the plaintiff Taylors against ChemRex for $395,250 (49% of the $775,000 total damages as found by the jury).

On appeal in *Taylor* I, the plaintiffs Taylor among other things assigned as error the trial court's submission of the comparative fault defense to the jury, while ChemRex cross-appealed, assigning as error the trial court's denial of its motion for directed verdict asserting there was insufficient evidence from which the jury could conclude that the ChemRex sales agent had apparent authority to give the oral or written warranties at issue. The court in *Taylor* I affirmed on the appeal and reversed on the ChemRex cross-appeal, concluding that there was not sufficient evidence for the jury to conclude that apparent authority existed on the part of the sales agent, thereby mooting or determining adversely the other assignments by both parties.

In *Taylor* II, the court reversed *Taylor* I, concluding there was sufficient evidence of apparent authority on the part of the ChemRex sales agent, and remanded the case for consideration of the assignments of error that had not been addressed, thus resulting in the further analysis and decision in *Taylor* III.

The *Taylor* III Decision

The *Taylor* III panel summarized the defendant ChemRex's three primary arguments in favor of applying a comparative fault analysis in defense of the contract warranty claims as follows:

> "On the merits, defendant relies in part on ORS 31.600, providing in part that "contributory negligence shall not bar recovery in an action * * * to recover damages for * * * injury to * * * property if the fault attributable to the claimant was not greater than the combined fault" of others; defendant contends that the statute's reference in part to "fault" rather than "negligence" demonstrates that it applies to claims other than negligence claims. Defendant also asserts that contributory negligence was a defense to a breach of express warranty claim under Oregon common law and notes that other jurisdictions recognize the defense in that context. Alternatively, defendant argues that plaintiffs' purchase of its stucco system constituted a sales contract that was governed by the Uniform Commercial Code (UCC); that their breach of warranty claim therefore constituted a claim for consequential damages arising from an injury to property proximately resulting from a breach of warranty, as provided in ORS 72.7150(2)(b); and that, under that provision, a buyer's remedy extends only to damages proximately caused by the breach and not to damages caused by the buyer itself or by third parties."

The *Taylor* III panel did not reach the first issue of interpretation of ORS 31.600. Instead, the panel based its decision on analysis of the UCC damages issue, concluding that, because "proximate" causation of damages under the UCC does not mean "sole" causation, the trial court properly submitted the defense to the jury, and regardless whether styled as "comparative fault" or "alternate causation". Pay close attention to the analysis used to justify that conclusion, as with no fanfare the *Taylor* III panel appears to have transmogrified the permissible defense of showing that alleged damages were not "proximately" caused by the defendant's conduct into a tort-based comparative fault approach to contract (at least UCC) damages in Oregon:

> "Under ORS 72.7140, where a buyer has accepted goods that are not as warranted by the seller, the buyer may recover as damages the loss resulting in the ordinary course of events from the seller's breach, measured as the difference between the value of the goods accepted and the value they would have had if they had been as warranted, as well as incidental and consequential damages. As pertinent here,

incidental damages include the costs of obtaining replacement goods or making repairs necessitated by the breach. ORS 72.7150(1); see, e.g., *McGinnis v. Wentworth Chevrolet Co.*, 295 Or 494, 502-04, 668 P2d 365 (1983) (discussing incidental damages). Consequential damages resulting from a seller's breach of warranty include "[i]njury to * * * property proximately resulting from" the breach. ORS 72.7150(2)(b).

Neither the cited provisions nor any other provision of ORS chapter 72 expressly provides that a buyer's recovery for losses resulting from a seller's breach of an express warranty is reducible by some measure reflecting wrongful conduct of the buyer or a third party. However, as the quoted provisions make clear, in order to recover damages for injury to property as provided in ORS 72.7150(2)(b), the buyer must demonstrate the existence of proximate cause between the seller's breach and the buyer's loss. See Larry Lawrence, *Anderson on the Uniform Commercial Code* § 2-314:612 (3d ed 1996-2002) (the conduct of the plaintiff is a defense to warranty liability to the extent that it shows that the proximate cause of the plaintiff's harm was not the breach of warranty). Thus, consequential damages do not include losses caused by the buyer or losses that the buyer could have prevented. See Patricia F. Fonseca and John R. Fonseca, *Williston on Sales* § 25:49 (5th ed 2006) (so stating; such damages "must have proximately resulted from the breach"); Lawrence, *Anderson on the Uniform Commercial Code* at § 2-715:70 ("In order for a buyer to recover a loss item as consequential damages, the buyer must establish that the loss was caused by the seller's breach."). "A cause may be 'proximate' as long as it substantially contributes to the ultimate harm, even if it is not the 'sole' or the 'but for' cause." Id. at § 2-314:618.

Here, in their second amended complaint, plaintiffs alleged in part that, as a result of defendant's breach of its warranty of the stucco system, plaintiffs incurred "[e]conomic damages in an amount not less than $1,100,000 for the remediation and repair of the subject hotel building, in order to restore the hotel building to the value and condition it would have had if the exterior stucco siding system and the product applied to the metal flashings had been as warranted by" defendant.(10) Those losses constitute damages – primarily consequential damages – for UCC purposes; accordingly, under ORS 72.7140 and ORS 72.7150, plaintiffs were required to show that the losses resulted from and were proximately caused by defendant's breach. Indeed, in arguing that plaintiffs' and Ramsay-Gerding's conduct was relevant to the question of its liability for plaintiffs' losses, defendant repeatedly contended that the issue of plaintiffs' and Ramsay-Gerding's "comparative fault" went to the element of causation.(11) We conclude that, whether the issue properly is characterized in Oregon as an issue of the parties' comparative fault or negligence, or as one of alternative or comparative causation, the trial court did not err in admitting evidence or instructing the jury on that issue, or in entering judgment and denying plaintiffs' motion for a new trial accordingly.

Moreover, in light of that conclusion, we need not decide whether ORS 31.600--providing that "contributory negligence" is not a bar to recovery of damages for injury to person or property if the "fault" of the plaintiff does not exceed the combined fault of other parties--is applicable to breach of warranty claims. See Lawrence, *Anderson on the Uniform Commercial Code* at §§ 2-314:649, 653 (most states have adopted comparative negligence statutes; some apply it to breach of warranty claims and some do not; those

that do in effect treat the issue as one of comparative causation or comparative fault)." Taylor III, *supra*, 233 Or App 272, at 288-91 (footnotes omitted)(emphasis added).

As of this writing, the parties in *Taylor* III have not sought reconsideration or review, but are expected to do so. The final chapter in that case may not yet be written.

The Implications of *Taylor* III

Our casual observer might ask whether, if it stands, the *Taylor* III decision will make any real difference in how construction disputes will be handled in Oregon. Is *Taylor* III limited in application to only UCC-based contract disputes? Does *Taylor* III sanction the routine submission of comparative fault verdict forms in contract disputes? Your author submits that trial courts might easily conclude the *Taylor* III analysis of UCC damages is equally-applicable to common-law contract damages. If so, regardless whether trial courts read *Taylor* III as authorizing comparative fault verdict forms, contract claimants will face more problems pursuing and collecting breach damages because of what would amount to a *sub-silentio* sea change in contract damage theory.

The *Taylor* III court's analysis may or may not hold up under scrutiny or on further review, and this discussion is not intended to explore or advocate among the competing legal or policy arguments as to the correctness of the *Taylor* III panel's analysis. However, to advance the discussion it bears reminder that applying the contractual "proximate cause" damage approach allows a claimant to recover from the other party under circumstances where the defendant was not the "sole" cause of the damages. From a policy perspective, this raises the initial question whether it necessarily follows, legally or logically, that because "solely" is a legal subset of "proximate" a court may or should alter long-established contract damages rules to focus on the narrower subset and thereby limit a breaching party's exposure only to those damages it "solely" caused.

Consider for a moment if *Taylor* III stands and is applied to common law contract disputes in the construction context.

In a traditional common law contract claim, the claiming party generally bears the burden of proving breach, proximate causation and foreseeable damages. Contract theory allows recovery from the breaching party of such damages as are required to place the injured party in the position it would have occupied if the breaching party had fully performed, provided the damage element was foreseeable and arose by reason of the breach. The defendant is free to introduce evidence that some or all of the elements or amounts of damage claimed were not "proximately caused" by the defendant's conduct. The jury is instructed on proximate causation, and returns a verdict that only involves the party/ies named as direct defendant(s) on the contract claim.

Under a tort-based comparative fault analysis, the defendant asserting the comparative fault defense, (let us refer to that party as the "primary" defendant), bears the burden of proving the identity and relative fault of each other entity it claims contributed to the damage. Generally, those "other entities" whom the primary defendant claims have some fault are joined as parties to the lawsuit, whether as third party defendants or in some other capacity. Other than as to settled parties or entities never joined as parties to the lawsuit, the comparative fault approach results in entry of a direct judgment in favor of the plaintiff against the primary defendant and each remaining party found to have fault for whatever share of damage was determined allocable to that party, and regardless whether the plaintiff asserted, or legally could have asserted, a claim against that party.

Whether the defense is termed "alternative causation" or comparative fault, how might the *Taylor* III rationale, if applied, affect the common scenarios we see every day in construction project dispute resolution?

First, how would the alternative causation/comparative fault approach to defense of contract claims intersect with the economic loss

rule (or what remains of it)? Despite *Abraham*, Oregon does not appear to have totally abandoned the economic loss rule. To the extent Oregon still requires contractual privity in order to assert certain claims, (such as for pure economic loss where no applicable standards exist independent of the contract), under an alternative causation/ comparative fault approach the damaged plaintiff could in theory obtain a direct judgment against any third party defendants to whom a percentage of fault is allocated even though the claimant could not assert a direct claim against those parties because privity is lacking. That result might be viewed by some as an improvement to our current system, at least in some circumstances.

Consider though that same scenario, trial of a contract claim by the project owner for purely economic loss (not property damage) where the defendant is the general contractor. The general contractor asserts a comparative fault defense, and one or more of those allegedly contributing to the loss are subcontractors or others which the defendant contractor has named as third party defendants. Using an alternative causation/comparative fault approach, the jury allocates a share of the fault to those non-parties, one or more of which is judgment-proof. In a normal contract dispute, the general contractor would be fully liable for the damages caused by its subcontractors and others below the contractor in the chain of contractual privity, so the collection risk falls on the defendant contractor. Applying an alternative causation/comparative fault analysis would in these cases shift to the plaintiff owner the risk of collection of any amount allocated to insolvent subcontractors, unless the re-allocation rules of ORS 31.610 come into play (generally, re-allocation is allowed only where the judgment-proof party's allocated fault equals or exceeds 25%).

Consider next the situation where the damaged party, such as a general contractor, caused the majority of its claimed loss (whether by its failure to mitigate or otherwise) and seeks recovery from one or more subcontractors that caused a portion of the loss. Under a normal contract approach, the plaintiff general contractor would assert its claim and the defendant subcontractors would assert mitigation or other defenses. The general contractor's recovery would be allowed according to the proof, and it would be irrelevant whether the contractor bore the majority of fault. Under an ORS 31.600 comparative negligence analysis, though, the general contractor would recover nothing if it was found to have caused at least 51% of its loss.

Consider also issues that would arise in trying to apply an alternative causation/comparative fault approach in arbitration of contract disputes, where other allegedly "at fault" entities cannot be joined as parties, such as because they have not agreed to arbitrate. Some might observe this may not substantially change the current scenario where the respondent is often faced with asserting its third party rights by arbitration with some and litigation with others, while being subject to the possibility of inconsistent results. Others might question how arbitration clauses on joinder and consolidation might be written, or how a given arbitration service's joinder and consolidation rules would be applied, so as to either facilitate or hinder the assertion of the defense.

In short, allowing a tort-based alternative causation/comparative fault defense to contract disputes would in many of today's ordinary dispute scenarios put a claimant at risk of being unable collect some portion, or even any, of its damages. Even though the burden of proof rests on the party asserting the defense, transforming "proximate" causation into "sole" causation represents abrogation of contract damage theory to the general benefit of defendants and the general detriment of claimants.

Does *Taylor* III represent a singular, fact-driven decision unlikely to have general application, or does Oregon now allow a comparative fault defense in any contract dispute? If the latter, can this mean the next logical step will be the further erosion or even abrogation of the economic loss rule to ameliorate some of the fallout?

Some of you may hold the studied view that any relaxation of the sacred privity requirement represents the figurative burning of an essential contract principle on the trial lawyer's altar to appease the gods of consumerist, pro-plaintiff sentiment. Others may equally sincerely believe that natural judicial evolution is moving too slowly toward fully removing theoretical barriers that have for too long prevented courts and juries from fully visiting upon every party the natural consequences of acts. Regardless where you stand, so long as *Taylor* III stands, practitioners and contracting parties cannot ignore its implications.

MERS AND FORECLOSURE ISSUES

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If your practice involves real estate in any way, then you are probably familiar with MERS. For the uninitiated, MERS stands for Mortgage Electronic Registration System, Inc. MERS' Web site (*www.mersinc.org*) states that "MERS was created by the mortgage banking industry to streamline the mortgage process by using electronic commerce to eliminate paper. Our mission is to register every mortgage loan in the United States on the MERS System." From a practitioner's standpoint, MERS allows banks to transfer mortgages among themselves without recording anything in the real property records.

A trust deed that involves MERS typically says that MERS is the mortgagee, although it also says "solely as nominee for Lender." The trust deed also has a MERS Identification Number (MIN) used by MERS and its affiliated lenders for tracking the mortgage.

So why would you care about MERS? If you plan to take any action against real property (such as foreclosure of a construction lien claim or a trust deed), MERS raises several issues that will affect your lawsuit. The most pressing questions are: (1) Who is the current lender? and (2) Should your foreclosure action name MERS as a party?

To use the example of a construction lien foreclosure, the usual practice is to obtain a judicial foreclosure guarantee policy from a title company. That policy will list the mortgagees of record for the parcel of real property. Let's say there is a single lender named "Generic Bank". You would name Generic Bank as a defendant in your foreclosure lawsuit. (If you are foreclosing a construction lien claim, you may even be asserting a senior priority over Generic Bank.) Typically, you might then receive a call or letter from counsel for Generic Bank, who informs you that Generic Bank transferred all of its interest in the mortgage to "Second Bank" quite some time ago. Assuming this is correct, does this raise the question of whether you have failed to name a necessary party to your lawsuit? See ORS 87.060(7).

A Kansas case illustrates some of these issues. In *Landmark National Bank v. Kesler.*, 216 P.3d 158 (Kan. 2009), the Kansas Supreme Court upheld its lower courts' rulings that MERS was not a necessary party to a foreclosure action by a senior lender. After the senior lender had served and taken a default against Millennia Mortgage Corp. (a junior lender whose trust deed involved MERS), both Sovereign Bank (a subsequent transferee of Millennia's junior trust deed) and MERS filed motions to set aside the judgment against Millennia. Sovereign and MERS claimed that, because neither was served, the default judgment could not be enforced because the plaintiff had not joined a necessary party. In finding that MERS was not a necessary party, the Kansas Supreme Court noted that MERS was not a real party in interest. The court also agreed with the trial court's finding that Sovereign's failure to register its interest with the county recorder precluded it from asserting its interests after the senior lender's foreclosure.

The Kansas Supreme Court expressly analyzed MERS' interests in the real property. The trust deed language quoted by the court is virtually identical to the language found in MERS trust deeds commonly recorded in Oregon. Showing a

sense of humor, the court described MERS' definition of the crucial words "as nominee for Lender" as similar to that used by "the blind men of Indian legend" describing an elephant.

The court concluded that MERS' relationship to the lender was "more akin to that of a straw man than to a party possessing all the rights given a buyer." The court noted that if MERS was correct that it had some rights separate from the lender's, then the mortgage may become unenforceable. The court cited several other courts from around the country that have reached that conclusion.

Finally, the court cited a Nebraska Supreme Court case in which MERS won a favorable decision that it was not a mortgage broker because it had no independent right to collect on the debt – in other words, the exact opposite position that MERS took in the case at issue.

In another matter, New York Chief Justice Kaye noted the following in a dissenting opinion: "Although creating efficiencies for its members, there is little evidence that the MERS system provides equivalent benefits to home buyers and borrowers – and, in fact, some evidence that it may create substantial disadvantages." *In re MERSCORP*, 8 N.Y.3d 90 (2006).

Despite the Kansas case, a careful practitioner would be well served to try to avoid such arguments by naming both MERS and the current trust deed holder in the construction lien foreclosure lawsuit (as well as the original lender named in the title report). While it may be easy to determine that MERS could assert an interest (if they are named in the recorded trust deed), how do you determine who might be a current trust deed holder? Fortunately, MERS itself has provided a web-based search engine (www.mers-servicerid.org/sis/) that purports to name the current lender. It is not clear whether the party found via the MERS search engine is the current mortgage holder or only the servicing company. However, it may be prudent to include that party in an abundance of caution.

A few other issues are outside the scope of this article but might be of interest to lenders' counsel. For example, does the subsequent trust deed holder have an obligation to defend and indemnify the initial trust deed holder? Part of that answer may lie in the documents between the two lenders when they transfer a mortgage through the MERS system. Another question is what if a transfer occurs but neither lender notifies MERS of the transfer? Does that affect any defense or indemnity obligations?

Another somewhat more practical question is whether to send to MERS the ORS 87.021 Notice of Right to a Lien, and/or the ORS 87.039 notice of filing lien claim, and/or the ORS 87.057 notice of intent to foreclose. Again, an abundance of caution may suggest that including MERS as a recipient of each notice is the prudent action.

In conclusion, the MERS system can produce a great deal of confusion. Practitioners need to decide whether naming MERS in their foreclosure actions is most beneficial for their clients.

[Thank you to Alan Brickley, Dan Duyck, and Doug Gallagher for their comments on this article.]

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PROPERTY TAX EXEMPTION FOR COMMERCIAL PROPERTIES UNDER CONSTRUCTION

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ORS 307.330 allows qualifying commercial properties under construction to be exempt from property tax if the application is filed by April 1. A property may qualify for exemption from property tax if the following requirements are met:

- ✓ The property "is being constructed in furtherance of the production of income" [ORS 307.330(1)(d), OAR 150-

307.330(2)(c), and *North Harbour Corp. v. Multnomah County*, 16 OTR 91 (2002)];

- ✓ Was in the process of construction on January 1 [ORS 307.330(1)(a) and OAR 150-307.330(2)(a)];
- ✓ For nonmanufacturing facilities, the facility cannot be occupied or used within one year from the date construction began [OAR 150-307.330(2)(e)]; and
- ✓ An application is timely filed with the assessor on or before April 1 [ORS 307.340].

The effect of the exemption is total. The assessor cancels the assessment against the new construction [ORS 307.340(1)], including the value or any machinery, equipment, and personal property located at the construction site which is or will be affixed to the building [ORS 307.330(2) and OAR 150-307.330(1)(c)]. The exemption does not include the value of the land. OAR 150-307.330(1)(a) and (2)(a).

For a manufacturing facility, the exemption may last as long as, but not more than, two consecutive years [ORS 307.330(1) and OAR 150-307.330(2)(b)], however a separate application must be filed for each year the exemption is claimed [OAR 150-307.340]. Typically, a "nonmanufacturing facility" is able to only claim the exemption for a single year. See ORS 307.330(1)(e), 307.340(1), and OAR 150-307.340.

The statute speaks as to exempting a new building, structure, or addition [ORS 307.330(1)] which includes all real property improvements erected upon the land and their appurtenances, including parking lots [OAR 150-307.330(1)(a)]. It is very clear that the exemption may be claimed through the renovation or expansion of an existing structure [OAR 150-307.330(1)(b)], so long as the construction is a major enlargement or modification. Additional stories or new wing will qualify for the exemption, as will the modification of a building to a new use. OAR 150-307.330(1)(b). A new storefront, modernization of an existing building, or installation of additional equipment will not support the exemption. OAR 150-307.330(1)(b).

Benchmarks exist as to when construction begins and ends. Demolition does not qualify as the start of construction [ORS 307.330(1)(e)]; neither does fill, excavation, grading, leveling, or any other element of site preparation [OAR 150-307.330(1)(a) and (2)(a)]. For practical purposes, the start of construction is marked by the laying of the foundation. OAR 150-307.330(2)(a). Construction ends when the building or structure is ready for use [OAR 150-307.330(2)(a)], with testing of operational systems considered as part of the construction process [OAR 150-307.330(2)(d)]. Actual occupancy and use of the premises is not required. OAR 150-307.330(2)(a). A use of part of the property will typically disqualify the entire property from the exemption. *Trendwest Resorts, Inc. v. Department of Revenue*, 340 Or 413, 134 P3d 932 (2006).

On January 1 the building, structure, or addition must be in the process of construction [ORS 307.330(1)(a)] which as a corollary means it must not be in use or occupancy on that date [ORS 307.330(1)(b) and (c) and OAR 150-307.330(2)(d)]. As the exemption is made as to income producing property, the test is one of commercial use or occupancy. OAR 150-307.330(2)(d). The construction period may, under some circumstances, include the period after completion of the building shell but prior to the building of the necessary tenant improvements. *Weston Holdings, LLC v. Multnomah County Assessor*, TC-MD 031039B (February 23, 2005).

The exemption must be applied for on or before April 1. There is no requirement that the assessor inform the property owner of the exemption. *Hayden Island Condos LLC v. Multnomah County Assessor*, TC-MD 060822D (August 18, 2008).

DEADLINE FOR LEGISLATION PROPOSALS

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Mitchell Law Office

If the Construction Section wishes to propose any legislative changes for the 2011 term, the deadline to submit those changes is April 1, 2010. Darien Loiselle is coordinating this for the Executive Committee. If you have any questions or proposals, please send them to Darien as soon as possible (*dloiselle@schwabe.com*).

Construction Law Section Executive Committee