

9/10/2014

STATE OF MICHIGAN
IN THE 20TH CIRCUIT COURT FOR THE COUNTY OF OTTAWA
SPECIALIZED BUSINESS DOCKET

414 Washington Street
Grand Haven, Michigan 49417
(616) 846-8320

L J & S DEVELOPMENT, LLC, a
Michigan limited liability company,

Plaintiff,

v

BOAR'S HEAD PROVISIONS COMPANY,
Inc., a Delaware corporation,

Defendant.

OPINION AND ORDER RE:
CROSS-MOTIONS FOR
SUMMARY DISPOSITION
2013-003511-CZ
Hon. Jon A. Van Allsburg

At a session of said Court held in the Ottawa County
Courthouse in the City of Grand Haven, Michigan,
on the 10th day of September, 2014.

PRESENT: Honorable Jon A. Van Allsburg, Circuit Judge

Plaintiff filed this declaratory judgment action to resolve a dispute between the parties whether defendant properly exercised an option to purchase real estate. Plaintiff purchased and developed the subject real property for use as a refrigerated warehouse by the defendant company, connected the building by a refrigerated tunnel with defendant's existing production facility on an adjoining parcel, and leased the development to the defendant. The lease agreement between the parties contained a detailed option to purchase. Defendant has exercised the option, and plaintiff contests the appraisal and the process by which the option price was determined. For the reasons stated below, plaintiff's motion for summary disposition is granted, and defendant's motion for summary disposition is denied.



Plaintiff moved for summary disposition pursuant to MCR 2.116(C)(8), (9), and (10), on the grounds that there is no genuine issue as to any material fact and that it is entitled to judgment as a matter of law. It asserts that defendant failed to comply with the express terms and conditions of the lease in exercising its option to purchase, and that defendant failed to comply with the lease's requirement that the appraisal be completed by an "independent third party appraiser." At the hearing on plaintiff's motion held on April 28, 2014, plaintiff limited its ground for summary disposition to MCR 2.116(C)(10). At the same hearing, the parties agreed to adjourn oral argument until August 25, 2014 (after the completion of discovery), and combine the hearing on plaintiff's motion for summary disposition with the hearing on defendant's anticipated motion for summary disposition.

Defendant then moved for summary disposition pursuant to MCR 2.116(C)(10), on the ground that plaintiff is estopped from asserting any defects in the appraisal process as a defense to defendant's counterclaim for specific performance of the option, and that defendant is entitled to judgment as a matter of law.

Summary of the Facts

The parties entered into a Lease on April 8, 2005, for a five-year term, with the right to extend the Lease for three, five-year renewal periods. The Lease was amended on January 1, 2009, in which defendant was permitted to rescind its August 1, 2008 exercise of the option to purchase. At the same time, the option to purchase was renewed and defendant exercised its first option to extend the lease for a five-year term.¹ Article 5 of the Lease contained a "Purchase

¹ The first renewal term was agreed to begin January 1, 2011 and end December 31, 2015.

Option.” For purposes of the present dispute, the relevant term of the Purchase Option is subparagraph 5.1(b), which reads as follows:

(b) The option price for the Premises² shall be as follows, subject to adjustment for customary closing apportionments, including without limitation, Rent, Taxes, fuel and water charges, and such additional adjustments as set forth in Section 5.1(c): (x) \$4,384,943.00 (such amount, the “Fixed Option Price”), if the Option is exercised during the period commencing on the first day of the Option Period and ending on the expiration of the 7th Lease Year and (y) if the Option is exercised at the expiration of the 8th Lease Year or at the expiration of any subsequent Lease Year, the option price shall be the fair market value of the Project³ on the date of the Option Notice (the “FMV Option Price”), as determined by an independent third (3rd) party appraiser selected by Tenant and at Tenant’s expense (the Fixed Option Price or the FMV Option Price, as adjusted, the “Purchase Price”). The choice of appraiser shall be subject to the approval of Landlord, which approval shall not be unreasonably withheld. A copy of such appraisal shall be sent to Landlord, if applicable, with the Option Notice, and such appraisal shall state in reasonable detail the basis of such fair market value determination.” (underlining in original).

Defendant initially exercised the option to purchase in 2008, but was permitted to withdraw that notice by mutual agreement of the parties. The 2009 amendment confirming that agreement provided that the option to purchase could be exercised only between September 1 and December 31 of each calendar year.

² Capitalized terms in the Lease have been specifically defined within the Lease itself. The terms “Premises” or “Property” are defined in Section 1.1(n) of the Lease, as “that certain real property located at 322 Roost Avenue, Holland, Michigan 49423, as more fully described on Exhibit A attached hereto and made a part hereof, together with all easements, rights, privileges and appurtenances thereto.” (Lease, p. 2) (underlining in original).

³ The term “Project” is defined in Section 1.1(o) of the Lease as “... the Property and all fixtures, improvements, appurtenances and installations located or to be located thereon during the Term hereof (inclusive of completed Landlord’s Work), as the same may be modified, altered or expanded from time to time in accordance with the terms of this Lease, but excluding any personal property or trade fixtures of Tenant.” (Lease, p.2-3). The term “Landlord’s Work,” as stated in Section 1.1(k) of the Lease, “shall have the meaning set forth in Article 4.” Article 4 of the Lease required Landlord, on the basis of agreed plans, to construct “a building containing approximately 44,880 square feet and a tunnel of approximately 2,725 square feet, together with the heat, ventilation and air conditioning system, other mechanical and electrical systems and systems for the distribution thereof throughout the structure, and other improvements on the Premises (collectively, the “Building”),” Section 4.1(i), p. 11 (underlining in original).

In 2012 Defendant retained American Appraisals Associates, Inc. (“American Appraisals”) to provide an appraisal of the Project.⁴ That appraisal was completed without consideration of the parties’ actual Lease, as defendant declined the appraiser’s request for a copy of it.⁵ On March 27, 2013, defendant requested that plaintiff approve its selection of American Appraisals to complete an appraisal.⁶ Plaintiff did not unequivocally respond,⁷ and on April 19, 2013 (about three weeks later), defendant’s counsel notified plaintiff that it had retained American Appraisals to conduct the appraisal.⁸ The actual appraisal work was performed in August 2013. Defendant’s counsel requested the right to review a draft of the appraisal before it was finalized, and instructed that the cover page of the draft was to be marked “attorney client work product – privileged.”⁹

The appraisal was completed as of September 3, 2013¹⁰, and defendant provided notice of its exercise of the option on October 14, 2013.¹¹ Defendant’s appraisal assigned a fair market value of \$1,980,000 to the Property, at a time when Plaintiff owed a mortgage balance on the property of \$3,300,000. The appraisal notes that the appraiser was aware of the tunnel that connects the Premises to the defendant’s neighboring manufacturing plant, but excluded it from

⁴ Summary Appraisal Report dated October 24, 2012 (BH000366-BH000416). This appraisal determined the market value of the fee simple estate of the subject property to be \$1,900,000. (BH000371).

⁵ Email exchanges of October 9, 2012 (AA000839-AA000840).

⁶ Letter from defendant’s counsel to plaintiff’s counsel (BH000098). It is undisputed that defendant did not disclose the existence of the 2012 appraisal.

⁷ Plaintiff denies that it approved, or that it unreasonably refused to approve, defendant’s choice of appraiser. Plaintiff’s Answer to Defendant’s Counterclaim, para. 14.

⁸ Letter from defendant’s counsel to plaintiff’s counsel (BH000096).

⁹ Email from defendant’s attorney to appraiser, August 7, 2013 (AA000494).

¹⁰ Summary Appraisal Report dated September 3, 2013 (AA000215-AA000279).

¹¹ Letter from defendant to plaintiff dated October 14, 2013 (BH000091-BH000092).

the appraisal.¹² Plaintiff disputes the FMV Option Price asserted by Defendant, for purposes of this motion, on two grounds: 1) The appraisal on which the asserted FMV Option Price is based cannot be used, as the appraiser selected by the defendant is not "independent" as that term is used in the Lease, and 2) the appraisal on which the asserted FMV Option Price is based cannot be used, as the appraisal fails to place a value on the entire Project as required by the Lease.

Standard of Review

Each party's motion under MCR 2.116(C)(10) tests the factual basis for the other party's pleadings. *Skinner v Square D Co*, 445 Mich 153, 161; 516 NW2d 475 (1994). "Summary disposition may be granted if the evidence demonstrates that there is no genuine issue with respect to any material fact, and the moving party is entitled to judgment as a matter of law." *Haliw v City of Sterling Heights*, 464 Mich 297; 627 NW2d 581 (2001), citing *Quinto v Cross & Peters Co*, 451 Mich 358, 362; 547 NW2d 314 (1996). In reviewing such a motion, this Court must consider the pleadings, affidavits, depositions, admissions, and any other admissible evidence in favor of the nonmoving party. MCR 2.116(G)(5). Granting the nonmoving party, the benefit of any reasonable doubt regarding material facts, this Court must then determine whether a factual dispute exists to warrant a trial. *Bertrand v Alan Ford, Inc*, 449 Mich 606, 617-618; 537 NW2d 185 (1995).

A party moving for summary disposition has the initial burden of supporting his position with affidavits, depositions, admissions, or other documentary evidence. The burden then shifts to the opposing party to establish that a genuine issue of disputed fact exists. If the burden of proof at trial would rest on the nonmoving party, the nonmoving party may not rely on mere

¹² Summary Appraisal Report dated September 3, 2013, p. 14 (AA000233).

allegations or denials in his pleadings, but must set forth specific facts which show that a genuine issue of material fact exists. If the opposing party fails to present documentary evidence establishing the existence of a material factual dispute, the motion is properly granted. *Quinto, supra*. A trial court may not make findings of fact in deciding a motion for summary disposition. *Jackhill Oil Co v Powell Production, Inc*, 210 Mich App 114; 532 NW2d 866 (1995).

Analysis

An option must be exercised in strict compliance with its terms. *Bowkus v Lange*, 196 Mich App 455, 459-460; 494 NW2d 461 (1992), rev'd on other grounds 441 Mich 930; 494 NW2d 461 (1993). An option is but an offer, strict compliance with the terms of which is required; acceptance must be in compliance with the terms proposed by the option both as to the exact thing offered and within the time specified; otherwise the right is lost. [*LeBaron Homes, Inc v Pontiac Housing Fund, Inc*, 319 Mich 310, 313; 29 NW2d 704 (1947), quoting *Bailey v Grover*, 237 Mich 548, 554-555; 213 NW 137 (1927), citing *Olson v Sash*, 217 Mich 604, 606; 187 NW 346 (1922).] The Michigan Supreme Court has held that substantial compliance is insufficient to exercise an option; rather “exact compliance with the terms of the option agreement” is necessary. *Beecher v Morse*, 286 Mich 513, 516; 282 NW 226 (1938). [Quoted from *Hunter Square Office Bldg, LLC v Paragon Underwriters, Inc*, unpublished per curiam opinion of the Court of Appeals (Docket No. 235115, May 20, 2003).¹³

I. Whether defendant’s appraiser is “an independent 3rd party appraiser” under the terms of the parties’ contract.

¹³ The court recognizes that it is not bound by this unpublished decision or the unpublished opinions cited later in this opinion, MCR 7.215(C)(1); *Charles Reinhart Co v Winiemko*, 444 Mich 579, 588 n 19; 513 NW2d 773 (1994), and merely views the cited opinions as persuasive, *Dyball v Lennox*, 260 Mich App 698, 705 n 1; 680 NW2d 522 (2003).

Defendant initially asserted that its appraiser is an agent of its attorneys, and that certain documents sought from the appraiser by the plaintiff are protected by attorney-client privilege and the work-product doctrine. However, after the court upheld defendant's assertion of attorney-client privilege and work-product, but questioned whether defendant could successfully assert that its appraiser was "independent" under such circumstances, defendant released some of the documents sought by the plaintiff.

Plaintiff asserts that American Appraisals is not an independent third party appraiser, for the reasons that 1) defendant limited the scope of the appraisal, 2) defendant's counsel reviewed, edited, and modified the appraisal before it was produced to the plaintiff, 3) defendant had ongoing business relations with American Appraisals, and 4) defendant asserts that the appraiser is an agent of its attorneys. Plaintiff further asserts that the appraisal is contractually inadequate as it fails to value the entire leased Project. Plaintiff contends that as a result of defendant's failure to comply with the terms and conditions of the option to purchase contained in the lease, the option has terminated and is of no further force and effect. Defendant responds that the appraiser is an independent third party appraiser despite the above allegations, because the defendant's prior relationship with the appraiser, and its counsel's contact with the appraiser, did not affect the appraiser's conclusion of value.

Whether plaintiff unreasonably withheld approval of defendant's choice of appraiser is a disputed fact. The parties also dispute whether defendant's appraiser provided "reasonable detail" for the basis of its fair market value determination. These disputed issues of fact are not appropriate for summary disposition.

II. Whether “fair market value” pursuant to the Option agreement requires a “leased fee appraisal.”

Counsel for both parties conceded at oral argument that “fair market value” and “market value” mean essentially the same thing. The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts. *United States v. Cartwright*, 411 U. S. 546, 93 S. Ct. 1713, 1716-17, 36 L. Ed. 2d 528 (1973) (quoting from U.S. Treasury regulations relating to Federal estate taxes, at 26 C.F.R. sec. 20.2031-1(b)).

The dispute between the parties arises from plaintiff’s argument that the fair market value MUST take into account the existing lease, as that represents a significant and relevant fact affecting the status of the property as of the date of valuation. Defendant argues that the valuation must be done without reference to the underlying lease. In fact, the appraiser requested, but accepted the refusal of defendant’s attorneys to provide, a copy of the lease when preparing the 2012 appraisal. A copy of the lease was later provided on August 13, 2013 while the 2013 appraisal was being prepared, with instruction that “the appraisal will be a fee simple appraisal and not a lease fee appraisal” (Email at AA000769-000771).

Both parties misstate the nature of the inquiry for purposes of establishing value. There is no single method of determining fair market value, and which method is most appropriate in a given valuation is a matter of judgment (unless otherwise required as a matter of contract). “The three most common approaches for determining true cash value are the capitalization-of-income approach, the sales-comparison or market approach, and the cost-less-depreciation approach.” *Great Lakes Div of Nat’l Steel Corp v City of Ecorse*, 227 Mich App 379, 390; 576 NW2d 667 (1998). In this case, the appraisal conducted in 2013 expressly addressed the various methods of

determining fair market value, and explains the appraiser's opinions with respect to the methods relied upon in the appraisal. The determinations made by the appraiser express opinions based upon disputed facts, and are not appropriate for summary disposition.

III. Whether the appraisal fails to place a value on the Project as required by the Option Agreement.

It is undisputed that the appraisal relied upon by the defendant does not include consideration of the refrigerated tunnel in its valuation. It is also undisputed that the "Project" referred to in the Option includes not only the real estate and its improvements, but also the "Landlord's Work," which expressly includes a refrigerated tunnel of 2,725 square feet and its attendant heating, cooling, air conditioning and mechanical and electrical systems (even though part of that tunnel is not located on – or under – the subject real estate). Defendant argues that both parties' experts in this case would conclude that the presence of the tunnel would *decrease* the value of the property as to any buyer other than the defendant, and would therefore decrease the *market* value of the property. Defendant goes on to argue that defendant is therefore overpaying for the property based on the appraisal as completed,¹⁴ and is free to pay more than the fair market value of the property resulting from that oversight. However, it was not the Property which had to be appraised; it was the Project which required appraisal.

The fundamental dispute in this case arises from the fact that real estate market values declined precipitously between the 2005 Lease and the 2013 exercise of the option. Plaintiff desires to avoid a massive financial loss (as its mortgage obligation is based on an amortization of the original construction cost, which is significantly higher than current real estate values), and Defendant desires to take advantage of the opportunity to acquire ownership of the property

¹⁴ For the reason that any third party buyer of the property – free of the lease – would have to close the tunnel to the adjoining property at significant expense.

at current real estate prices and avoid an ongoing significant rental expense (which is also based upon the original construction cost). The option contained in the Lease effectively allocated the risk of an increase or decrease in market value between the parties. During the early years of the lease, that risk was on the defendant, as the option price was predetermined and fixed (although defendant retained the choice whether or not to exercise it). After the seventh year of the lease, however, the option price was no longer fixed, but was based upon fair market value. The risk of a market decline at that point was clearly allocated to plaintiff.

The option agreement contained in the lease does, however, provide some protections to plaintiff. The agreement requires that the fair market value be determined by 1) an independent third party appraiser, 2) who is approved by plaintiff (provided approval may not be unreasonably withheld), 3) the appraisal must provide “reasonable detail” as to “the basis of such fair market value determination,” and 4) must appraise “the Project,” and not simply the “Property.” The Lease agreement defines these terms, as stated in the footnotes above. The appraisal prepared by American Appraisal and relied on by the defendant clearly appraised the Property at issue, but did not appraise the “Project.” The appraisal specifically excludes the 2,725 square foot refrigerated tunnel from the scope of the appraisal, but the tunnel is expressly included in the scope of the Project as part of the Landlord’s Work.

Defendant argues that plaintiff is estopped from asserting its failure to strictly comply with the terms of the option agreement. This argument was considered in *Hunter Square, supra*, and rejected:

“In essence, plaintiff uses the doctrine of equitable estoppel to affirmatively establish its contract claim. Equitable estoppel, however, may not be used to affirmatively establish a cause of action. ... Defendant argues equitable estoppel

could not apply because both parties were not mutually bound. ... More accurately, defendant could not by its unilateral conduct modify the required mode of exercising its option. Indeed, as plaintiff recognizes, because it granted the option, it could insist on strict compliance with the required manner and mode of exercise, despite any conduct by defendant to the contrary. Only plaintiff could waive strict compliance of the requirement of exercising the option....” *Id.*, at slip op., p5 (citations omitted).

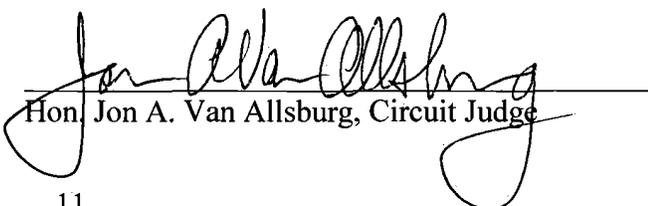
The Court of Appeals concluded that it was not inequitable to enforce “the plain terms of the parties’ contract.” *Id.*, at slip op., p6. As it is undisputed in the present case that defendant did not strictly comply with the terms of the option agreement, it cannot enforce the option agreement.

IT IS HEREBY ORDERED AND DECLARED as follows:

1. The October 14, 2013 purported exercise of Option by Defendant failed to strictly comply with the terms of the Option as set forth in the Lease, and Plaintiff was not obligated to accept it. Plaintiff’s motion for summary disposition is GRANTED. Defendant’s cross-motion for summary disposition is DENIED.
2. Plaintiff has no obligation to proceed with closing based on the valuation contained in the American Appraisal Report as it did not appraise the Project as required by the terms of the Option. Whether the Report was prepared by an “independent third party appraiser,” whether plaintiff unreasonably withheld approval of defendant’s choice of an appraiser, and whether the appraiser provided “reasonable detail” for the basis of its fair market value determination are all disputed issues of fact which are not decided in this opinion.
3. Except as stated above, the Lease shall remain in full force and effect.
4. Plaintiff’s request for its costs, expenses, and reasonable attorneys’ fees in connection with this action is reserved for post-judgment evidentiary hearing. Plaintiff may file a motion for attorney fees and costs with a brief in support, showing the basis for the request and the reasonableness of its claim in accord with *Smith v Khouri*, 481 Mich 519; 751 NW2d 472 (2008).

IT IS SO ORDERED.

Dated: September 10, 2014


 Hon. Jon A. Van Allsburg, Circuit Judge