Fall 2007

Doctrines of Waste in a Landscape of Waste

John A. Lovett

Follow this and additional works at: http://scholarship.law.missouri.edu/mlr

Part of the Law Commons

Recommended Citation

Available at: http://scholarship.law.missouri.edu/mlr/vol72/iss4/8
Doctrines of Waste in a Landscape of Waste

John A. Lovett*

I. INTRODUCTION

One of the virtues of William Stoebuck and Dale Whitman’s seminal hornbook, *The Law of Property*, is its extensive treatment of the subject of waste.1 Using half of a chapter, Stoebuck and Whitman introduce their readers to one of the great subjects of the common law of property, one that attracted the attention of Coke,2 Blackstone,3 Kent,4 and many others. Their detailed analysis of the subject, which provides a general historical overview, a discussion of the seminal voluntary waste cases, Melms v. Pabst Brewing Co.,5 and Brokaw v. Fairchild,6 and a presentation of the legal and equitable remedies for waste, may strike some readers as old-fashioned.

Although one recent law review article has called attention to several early nineteenth century waste cases,7 relatively little contemporary academic scholarship has addressed waste doctrine in depth. That does not mean, however, that the subject has completely gone out of fashion. Practice-oriented treatises, such as the latest edition of *Powell on Real Property*, still give considerable attention to waste.8 And virtually every property law hornbook or case book will offer some treatment of waste. Some only devote a few short

---

*Associate Professor, Loyola University New Orleans College of Law.


3. WILLIAM BLACKSTONE, 3 COMMENTARIES *223, *281-82.

4. 4 JAMES KENT, COMMENTARIES ON AMERICAN LAW 74-80 (12th ed. 1873) (1830).

5. 79 N.W. 738 (Wis. 1899).


8. 4 POWELL ON REAL PROPERTY ch. 56 (Michael Allan Wolf ed., 2000); see also 2-4 THOMPSON ON REAL PROPERTY, §§ 19.07-19.09, 22.06(a), 31.07, 32.07 (David A. Thomas ed., 2d Thomas ed. 2004) (treating waste issues in context of life estate, reversion, remainder, joint tenancy and co-tenancy).
paragraphs to the subject, as typified by a popular student-oriented treatise. Others offer one complete waste case (often the chestnut *Baker v. Weedon*) and notes about the doctrine in other contexts. And some casebooks attempt much more detailed treatments of waste and offer two, and sometimes even three or four, full cases and weave discussions of waste throughout their presentations of other traditional doctrinal categories.

What do the casebook authors say about waste? Typically they make three kinds of observations. First, they suggest that waste conflicts (and the


10. 262 So. 2d 641 (Miss. 1972).


12. The casebooks with perhaps the most extensive treatments of waste are A. JAMES CASNER ET AL., CASES AND TEXT ON PROPERTY 152-56, 353-60, 467-73, 556 (5th ed. 2004) (offering four waste cases, one involving an assertion of a prescriptive easement against a landlord, another addressing a life tenant’s duties with respect to casualty insurance proceeds, a third on the duty of a life tenant to pay real estate taxes, yet another ameliorative waste case involving a landlord and tenant, and finally a note about waste among co-tenants); EDWARD H. RABIN ET AL., FUNDAMENTALS OF MODERN PROPERTY LAW 233-49 (5th ed. 2006) (devoting an entire chapter and three cases to waste issues in the context of life estates); PAUL GOLDSTEIN & BARTON H. THOMPSON, JR., PROPERTY LAW: OWNERSHIP, USE AND CONSERVATION 634-46, 539, 754, 774 (2006) (offering waste an entire chapter unit and two cases (*Moore* and *Baker*) and discussing it in other contexts as well); JON W. BRUCE & JAMES W. ELY, JR., MODERN PROPERTY LAW, 39-45 (5th ed. 2003) (offering two waste cases in the context of landlord and tenant relationships); and not surprisingly, GRANT S. NELSON, WILLIAM B. STOEBUCK, & DALE A. WHITMAN, CONTEMPORARY PROPERTY 286-304 (2d ed. 2002) (offering a detailed introduction, *Brokaw* and *Baker*, and a long note introducing the time value of money).
difficult fact intensive and subjective inquiries they require) are generally a thing of the past, a problem that well-trained and attentive lawyers can easily avoid for their clients by creating trusts rather than legal life estates. Second, and almost as commonly, they use waste cases to begin teaching students basic law and economics principles. For example, a waste conflict will be staged as a dispute between a present estate holder and future interest holder, with the former seeking to maximize short term economic value and impose externalities on the latter either by depleting resources like timber or neglecting to make necessary repairs. Or a waste conflict will emerge when a future interest holder seeks to use a bilateral monopoly position to extort inefficient concessions from the present interest holder, a situation that the ameliorative waste doctrine should ideally remedy. Third, and much less frequently, casebook authors raise questions about how a grantor of a temporally limited possessory estate and a future interest might have intended for the parties to resolve a waste conflict. As important as these pedagogical statements may be, more questions arise. What do law professors and jurists say to each other when they write about waste in other settings? And how do courts explain their waste decisions to parties? I will return to these questions later.

While I do not deny that classic waste cases – conflicts between life tenants and future interest holders over alleged instances of voluntary waste – are less common today than they used to be (but perhaps not as uncommon as some might think), my goals in this article are to reawaken readers to the importance of waste doctrine, to suggest that the great days of waste may not be completely in the past, to recommend some new uses for waste cases as teaching tools, and generally to urge a renewed appreciation for waste – an appreciation that Dale Whitman, for one, never lost. Although I do not deny the urge to review all of the great moments in the development of waste doctrine, in this article I will focus only on what a few leading interpreters (legal academics and other law professionals) say about waste when they talk to each other and comment on two recent clusters of cases where waste doctrines and other closely related rules are currently at play. My primary but

13. See, e.g., DUKEMINIER, supra note 11, at 204 (suggesting that waste problems can and should be avoided by substituting trusts for legal life estates); SINGER, supra note 11, at 557 (same); SMITH, supra note 11, at 395 (same); FREYERMUTH, supra note 11, at 262-63 (same); GOLDSTEIN & THOMPSON, supra note 12, at 646 (same). The authors of the Casner text make a slightly different point, advising students who draft or review an instrument creating a life estate to pay careful attention to the provisions spelling out the life tenant's responsibilities for repair to avoid permissive waste problems. CASNER, supra note 12, at 355.

14. See, e.g., FREYERMUTH, supra note 11, at 260-61; SMITH, supra note 11, at 382; GOLDSTEIN & THOMPSON, supra note 12, at 638, 641; CHUSED, supra note 11, at 865-69.

15. FREYERMUTH, supra note 11, at 260-61.

16. See infra notes 97-98 and accompanying text.
not exclusive focus is on voluntary or commissive waste cases because they tend to reveal the most difficult problems and the sharpest conflicts.

In the end I hope to show not only that doctrines of waste still matter, but also that they matter especially in what I call “landscapes of waste,” that is, in settings in which some kind of dramatic, and relatively sudden physical, environmental or economic transformation has taken place. In other words, I claim that waste doctrine becomes particularly important in moments of radical change when patterns of land use and development are under intense pressure because the physical, environmental, social and economic circumstances affecting the underlying property relationship are changing dramatically. Put simply, we tend to think of waste doctrine as a relatively stable background principle in property law that lends certainty to property relationships and is susceptible to and generative of efficient private ordering. Yet I suggest that in moments of rapid and profound change courts and legislators not only confront difficult questions about waste, but are often tempted to abandon bright line versions of waste doctrine and muddy it in spasms of doctrinal transformation.  

II. INTERPRETATIONS OF WASTE DOCTRINE

A. Of Life Estates: The Restatement of the Law of Property (1936), Stoebuck & Whitman, and Merryman

There has always been a tension in waste doctrine between a purely economic understanding of what constitutes waste – one that measures waste by looking for a diminution in the market value of the property – and an understanding based more on the normative prerogative of the future interest holder to decide what kind of changes can be made to the property. We might say this tension is between a purely utilitarian understanding of waste and a social understanding of waste. In 1936, at the time the first Restatement of Property was crafted, this tension was especially apparent because of the then recent and much criticized decision in Brokaw v. Fairchild. In this case, a New York court, pointing in part to the exclusive prerogative of several contingent remaindersmen to exercise “acts of dominion or ownership,” enjoined a life tenant from demolishing a palatial residence on Manhattan’s Upper East Side.

17. I explore the interplay between events causing dramatically changed social, economic and environmental conditions to arise and property law in John A. Lovett, Property and Radically Changed Circumstances, 74 TENN. L. REV. (forthcoming 2007).

18. See generally Purdy, supra note 7. See also infra notes 103-13 and accompanying text.

Not surprisingly, the first Restatement of Property reflected this tension by adopting two seemingly conflicting definitions of actions that could constitute voluntary waste. First, in section 138 the Restatement declares that a life tenant has a duty not to diminish the "market value" of the subsequent interests. Then section 140 imposes on the life tenant "a duty not to change the premises, as to which the estate for life exists, in such a manner that the owners of the interests limited after the estate for life have reasonable ground for objection thereto." The conflict arises because a literal reading of these two sections might suggest that a subsequent interest holder can object to and block changes in the use of the property proposed by a life tenant, even if those changes do not diminish the property's market value, as long as the objections to the changes are "reasonable." In other words, the "reasonable objection" standard in section 140 might override, or at least undermine, the market value measurement of waste in section 138.

These two conflicting Restatement rules on voluntary waste can be reconciled, however, by focusing on changed circumstances. As Professors Stoebuck and Whitman explain in their treatise, the Restatement's drafters were trying not only to state the general rule for changes to premises articulated by the Wisconsin Supreme Court in Melms but also to respond to the facts presented in Brokaw and its much derided result. Thus, the backbone of these provisions is found in comment (f) to Section 140, which, synthesizing Melms and the dissent in Brokaw, states that subsequent owners should have "no reasonable ground for objection" to a proposed alteration or replacement of a structure (or presumably some other change in the premises):

when a substantial and permanent change in the conditions of the neighborhood in which the land is located has deprived the land in its existent form, of reasonable productivity or usefulness; and the proposed alteration or replacement is one which the owner of an estate in fee simple absolute normally would make; and the owners of the interests limited after the estate for life are either not subject to financial liability or are adequately protected against financial liability arising from the proposed construction operations.

20. STOEBUCK & WHITMAN, supra note 1, § 4.2, at 151.
22. Id. § 140 (emphasis added).
23. STOEBUCK & WHITMAN, supra note 1, § 4.2, at 151-52.
24. Id. at 152.
25. RESTATEMENT (FIRST) OF PROP. § 140 cmt. f (emphasis added).
It is important to recollect here the key holding in *Melms v. Pabst Brewing Co.*,\(^{26}\) in which the Wisconsin Supreme Court rejected several reversioners' damage claim for waste arising from the destruction of a once fine residence whose surrounding neighborhood was transformed into an industrial zone of Milwaukee. In *Melms*, the court specifically held that a life tenant is entitled to make substantial alterations in a structure or even to demolish it, absent a contractual obligation to restore the property to the condition in which it was received, "when . . . there has occurred a *complete and permanent change of surrounding conditions*, which has deprived the property of its value and usefulness."\(^{27}\) In other words, the key factor that reconciles the conflicting Restatement provisions is the phenomenon of changing conditions in the neighborhood. Put differently, a mere increase in market value alone might not justify allowing a life tenant to make fundamental changes in the form or use of property subject to a life estate in a static environment. But when a "permanent and substantial change in the condition of the neighborhood" has occurred, a life tenant can make responsive changes as long as they do not diminish the property's market value.

Before leaving the realm of life estates, it is also useful to recall what John Merryman has to say about waste in his illuminating two chapters on the subject in *The American Law of Property*.\(^{28}\) Not only does Merryman, writing in 1952, construct a clever taxonomy of the various approaches to waste, but, like Stoebuck and Whitman, he also highlights the importance of changed conditions. In his taxonomy, Merryman first points out that some cases, texts and statutes adopt what he calls "a mnemonic approach," one that blindly attaches liability for waste to certain acts - e.g., cutting and selling timber or changing the land's use - regardless of context. This approach, he complains, results from a "too literal application" of Coke and does not accurately represent the law in England or anywhere.\(^{29}\) In essence, Merryman seems to be describing and critiquing here an understanding of waste based on the social prerogative of the future interest holder or at least the arbitrary choices of the life estate grantor. Second, Merryman observes in other cases a "functional approach," one in which acts are held to constitute waste only when they "prejudice[] the inheritance."\(^{30}\) He criticizes this nakedly utilitarian approach as being too circular and mechanical and for relying on the dubious assumption that creators of life estates intend land to pass to subsequent interest holders completely undiminished.\(^{31}\) In fact, this functional approach only makes sense for Merryman when it is understood in terms of the last and, for him, most refined approach, the "intention approach," one which

---

26. 79 N.W. 738 (Wis. 1899).
27. *Id.* at 741 (emphasis added).
29. *Id.* § 20.1, at 71-72.
30. *Id.* at 72.
31. *Id.* at 72, 74.
demands a search for the implied intention of the grantor or the parties who created the life estate.\footnote{Id. at 72-74.}

Crucially for our purposes, Merryman restates this “intention approach” in terms reminiscent of section 140 of the Restatement of Property: the grantor must be assumed to have intended “that the tenant be allowed to use land in a \textit{reasonable manner to accomplish the purpose} of his tenancy.”\footnote{Id. at 73 (emphasis added).} Conversely, the grantor must have intended for the subsequent interest holder to receive his or her land at the end of the life estate, not in an unaltered state, or even in a state with equivalent or enhanced market value, but only “substantially undamaged” by the use and enjoyment of the life tenant.\footnote{Id.} Thus, the best approach for resolving waste conflicts for Merryman is a broad and flexible “reasonable use” standard, one that allows a judge to consider not only the changed market value of the property, but also standards of conduct imposed under the instrument creating the estate, community customs, public policy requirements as discerned by the judge, and, most important of all, \textit{new conditions and circumstances surrounding the proposed use}.\footnote{Id. § 20.11, at 94-96. \textit{See also} id. § 20.5 (elaborating on judge’s rule in discerning public policy needs at the time of the proposed use).} In fact, chief among Merryman’s numerous reasons for supporting this flexible standard is its tendency to allow for contextual judging – giving courts room to consider geographic variations and effects on land, not just dry legal interests in land – and to allow for reasonable adaptation when circumstances have changed since creation of the life estate.\footnote{Id. § 20.2, at 77-80. Merryman emphasized this last rationale forcefully, arguing that determinations about reasonable use must be made “with reference to the conditions existing at the time and under the circumstances of the proposed use.” \textit{Id.} at 79.} Indeed, like so many of his generation, Merryman was troubled by the decision in \textit{Brokaw} precisely because of the court’s failure to consider the compelling change in circumstances that the life tenant pointed to as a justification for the proposed demolition of the Brokaw mansion and its replacement with a modern apartment building.\footnote{Id. § 20.11, at 98.} In sum, this initial foray into the doctrine of waste in the context of life estates reveals that changing circumstances are at least a significant factor, if not the crucial one, in explaining why courts and legal commentators seek more flexible, muddier standards for deciding what is actionable voluntary waste.
Turning now to voluntary waste in the context of leases, we continue to see the impact of changed conditions on the formulation of waste standards but we also become more aware of the role of private ordering in responding to ambiguity in default waste standards. Here I draw lessons from another Restatement and from a classic treatise, Friedman on Leases, originally authored by New York attorney Milton J. Friedman in 1954 and recently updated by Patrick J. Randolph. Although the famous Melms and Brokaw decisions both involved life estates, Friedman, like so many other mid-twentieth century commentators, felt obliged to address them. He did so first because courts confronting landlord-tenant disputes about improvements and alterations tended to borrow freely from life estate waste cases given the relative scarcity of lease waste cases. In addition, Friedman did not view the Brokaw decision as particularly unfortunate, at least not the way John Merryman and other contemporary critics did. In fact, for Friedman, the Melms case appears to have been the true outlier decision. What accounts for this dissenting interpretation that seems comfortable with a more “mnemonic” approach to waste?

First, Friedman points out that the different procedural posture of the two decisions may have justified the New York Supreme Court’s apparently harsh ruling in Brokaw. Friedman here claims that it makes sense for a court, as in Brokaw v. Fairchild, to employ a relatively strict rule for deciding ex ante whether a life tenant can make a drastic change in the use of the property subject to a life estate. Conversely, as in Melms v. Pabst Brewing Company


40. In addition to Merryman's criticism in AMERICAN LAW OF PROPERTY, supra note 28, §20.11, at 98, the Brokaw decision, and its threat of re-introducing a strict, English style rule on voluntary waste, prompted a flood of academic criticism. See Marvin L. Niehuss, Alteration or Replacement of Buildings by Long-Term Lessee, 30 MICH. L. REV. 386, 397 (1932); Note, Liability for Ameliorative Waste, 43 HARV. L. REV. 1130 (1930); 2 HERBERT THORNDAKE TIFFANY, REAL PROPERTY § 632 (3d ed. 1939).

41. In Brokaw v. Fairchild, 237 N.Y.S. 6, 9-11 (1929), the life estate holder had petitioned the court to obtain approval ex ante to engage in an act of intentional waste—demolition of the venerable Brokaw mansion and its replacement with a thirteen story, 172 unit apartment building.

42. In Melms v. Pabst Brewing Co., 79 N.W. 738, 739 (Wis. 1899), the reversioners brought an action ex post to recover damages for an accidental act of waste.
when the waste issue merely concerns what damages may be awarded *ex post* after a substantial change has already taken place, a more utilitarian and exclusively market value based standard is more appropriate. For Friedman, this different procedural posture partially justifies the *Brokaw* court’s decision to employ a higher standard of proof to establish an exception to the standard rule for waste than in *Melms*.\(^43\)

Second, and just as important, although a significant change in surrounding land use patterns had occurred and the carrying and maintenance costs had grown more burdensome since the granting of the life estate in *Brokaw*, still for Friedman, as for the court, the *Brokaw* mansion remained much more suitable to its surroundings than was the case in *Melms*. As a result of this factual difference, Friedman suggests that the court was correct in assuming that the testator would have intended that the building be preserved in these more ambiguously changed circumstances.\(^44\) In short, there was simply not such a drastic change in the surrounding conditions in *Brokaw* as in *Melms*.

Given this interpretation of the *Melms* and *Brokaw* decisions, it is not surprising that Friedman would conclude, at least in the landlord-tenant context, that the “classic view” of waste – as prohibiting *substantial* and *permanent* tenant alterations or improvements to a building or land without the landlord’s consent, regardless of whether they enhance the value of the landlord’s estate – has been firmly adhered to throughout most of the nineteenth and twentieth centuries in a remarkably wide variety of fact patterns.\(^45\) In Friedman’s view, it is only the exceptional case like *Melms*, or other unusual

---


\(^{44}\) Id. at 22-8. Indeed, other mansions remained in the vicinity of the *Brokaw* mansion and the contrast between a mansion and apartment buildings on the upper East Side of Manhattan was simply not as great as that between mansions and an industrial-commercial zone of Milwaukee. *Compare Melms*, 79 N.W. at 739, with *Brokaw*, 237 N.Y.S. at 18.

\(^{45}\) FRIEDMAN & RANDOLPH, supra note 38, § 22:1.4 (citing numerous authorities). Cf. Sigsbee Holding Corp. v. Canavan, 240 N.Y.S.2d 900 (Civ. Ct. 1963) (holding that a residential tenant did *not* commit waste by replacing old, used cabinets with new ones because this change did not produce an injury to the reversion but rather “enhanced its value” and did not constitute a “*substantial* and *permanent* change in the nature and character of the building premises”) (emphasis added); Gabin v. Goldstein, 497 N.Y.S.2d 984 (Civ. Ct. 1986) (after tenants abandoned, landlord awarded $1,500 for cost of removal of built-in furniture installation in single family home rented by absentee owner to tenant under four year lease).
lease cases with stark examples of unmistakable and lasting tenant enhancements to land,\textsuperscript{46} that seem to buck this trend.

The provisions of the 1977 Restatement of the Law of Property (Second): Landlord and Tenant concerning tenant duties in relation to the physical condition of leased property echo Friedman’s more traditional static approach to waste yet also reveal a desire for more flexibility. Section 12.2(1) states that, in the absence of contractual agreements, a tenant is entitled “to make changes in the physical condition of the leased property which are reasonably necessary in order for the tenant to use the leased property in a manner that is reasonable under all the circumstances.”\textsuperscript{47} In contrast to this flexible reasonableness standard that is relatively open to tenant initiated changes during the term of the lease, section 12.2(3) imposes on the tenant a strict duty to restore the premises to their original condition at the end of the lease if the tenant has made “permissible changes,” unless (a) the lease provides otherwise, (b) restoration is impossible, (c) the changes are the result of normal wear and tear, or (d) “it would be unreasonable to require the restoration in light of the probable future uses of the property.”\textsuperscript{48}

On one hand this default restoration obligation seems to mirror the rigid traditional voluntary and permissive waste standards focused on preserving the pre-lease condition of the property for the sake of the long-term interests of the landlord. At the same time, though, the invocation of a reasonableness limit on restoration liability in subsection (3)(d) seems to leave the field open for more unpredictable ex post decision making about the precise limits of the post-lease restoration duty if the tenant’s changes are conceivably consistent with the future use of the property in light of some intervening change in circumstances or because the tenant’s changes actually improved the property’s underlying value.\textsuperscript{49} In short, it seems as if the Restatement drafters were uncertain about how to balance the conflicting policy goals of certainty and flexibility in the lease waste context or at least sought to establish differ-

\textsuperscript{46} See, e.g., J.H. Bellows Co. v. Covell, 162 N.E. 621 (Ohio Ct. App. 1927) (holding that, in the context of a twenty-five year lease for development of a golf course, with a renewal option for another ten years, the tenant’s draining of a stagnant shallow pond and converting it into a smaller but deeper lake accessible by boat from Lake Erie did not constitute waste).

\textsuperscript{47} \textsc{Restatement (Second) of Prop.: Landlord and Tenant} § 12.2(1) (1977) (emphasis added).

\textsuperscript{48} Id. § 12.2(3). See also id. cmts. n, o (elaborating on restoration duties).

\textsuperscript{49} The Restatement’s illustration of this point is illuminating:

L leases office space to T for five years. T installs a central heating and air conditioning unit, which has vents running through the walls into the individual rooms. L will not be handicapped in renting the office space in the future by such installations and hence T is not required to remove them under the rule of subsection (3), even if L requests their removal.

\textit{Id.} § 12.2 illus. 27. But what result if future tenants determine the installed HVAC system is outmoded and inefficient?
ent default waste standards for different moments in the lessor-lessee relationship. We will return to the problem of establishing waste standards for complex lease relationships when we consider a waste controversy currently roiling Louisiana.

Finally, it is worth noting Friedman's reaction to the seemingly flexible reasonableness standard that was adopted by the New York legislature in response to the infamous Brokaw decision. This New York statute allows a life tenant with a life expectancy of at least five years or a tenant under a lease with an unexpired term of at least five years to apply to a court to alter or replace an existing structure and provides that the court should grant approval if the proposed alteration or replacement is one that a prudent owner would make, it would not reduce the market value of the reversion, the tenant provides security to assure completion of the project and protect the reversion holder from being responsible for its cost, and the proposed alteration or replacement does not violate the terms of any agreement regulating the tenant's conduct. Although this seems like an admirably judicious piece of legislation, carefully calibrated to right the wrong perpetrated in Brokaw through its incorporation of both a prudent owner and market diminution standard, it apparently has rarely been litigated, let alone used or copied by other states. Why this indifference? According to Friedman, the answer is that its potential for ex post uncertainty, combined with the harsh vestiges of the strict common law rule prohibiting voluntary changes in leased premises in situations beyond the scope of the statute, has induced most commercial landlords and tenants (in New York at least) to pay close attention to the issue of substantial alteration and improvement of the leased premises and negotiate and draft specific contract language addressing the problem.

If we take a broad view of waste at this point, we see that in relationships involving possessory and future interest holders that are either finite in duration or originate in voluntary contractual agreements (e.g., leases), as opposed to involuntary and more temporally indefinite grants made by testators or donors (e.g., life estates), courts tend to employ relatively strict and crystalline rules governing voluntary waste. In addition, the rigidity of


52. FRIEDMAN & RANDOLPH, supra note 38, § 22:2.1, at 22-11 (noting that most lease stipulations forbid all alterations and improvements without the landlord's consent and that courts generally recognize landlords' rights to enforce such stipulations arbitrarily).

53. See STOEBUCK & WHITMAN, supra note 1, § 4.3, at 153 (observing that "the rules as to what constitutes waste on the part of tenants for years (and periodic tenants) are somewhat more restrictive than those applicable to life tenants").
these judicial rules seems to induce private ordering as parties frequently negate common law or statutory default rules on waste by adopting their own contractual terms. Put differently, there seems to be greater toleration for allowing courts to readjust a property relationship to take into account significant and perhaps unanticipated changes in surrounding conditions when the relationship is more long term and open ended in duration and scope or when parties find themselves wedded to each other because of the decisions of others rather than through their own conscious contracting. Conversely, when property relationships have clearly defined durations and originate in open eyed contract negotiation, waste rules remain more inflexible and mnemonic. These seem to be the lessons that the first two property Restatements and Milton Friedman teach us about waste. When we examine the problem of mineral leases in Part III, however, we will find that these common sense predictions are not always true.


Turning now to waste doctrine in the context of mortgages, we see how sudden changes in circumstances can again create waste conflicts and how the tendency of parties to engage in detailed private ordering in anticipation of waste can both exacerbate and alleviate those conflicts. We begin here with section 4.6 of the Restatement of the Law of Property (Third): Mortgages, which recognizes that a mortgagor can commit waste by any number of actions or omissions – by making physical changes to the mortgaged property that reduces its value, by failing to maintain or repair the mortgaged property, by not paying property taxes or not complying with maintenance, construction, demolition or insurance covenants in the mortgage, and even by retaining rents which the mortgagee is entitled to possess.54 Although the rationales for recognizing waste in the mortgage context can vary depending on whether a state adopts a lien or title theory approach to mortgages,55 the underlying concern everywhere should be, according to Professors Nelson and Whitman (the principal drafters of the Restatement (Third) of Property: Mortgages), determining “what constitutes an impairment of the security.”56

55. In a title theory state, a mortgagor is analogized to a tenant of the mortgagee and thus when a mortgagor engages in impermissible uses of the mortgaged property, the mortgagee can bring an action in trespass (for instance when a building is removed) or an action to recover for any damage to his legal property interest, regardless of whether the mortgagor’s conduct caused any degradation in the mortgagee’s security position. GRANT S. NELSON & DALE A. WHITMAN, REAL ESTATE FINANCE LAW § 4.4, at 140-41 (4th ed. 2001). In a lien theory state, the focus is instead on “impairment of the security interest, not upon the damage to the property itself.” Id. § 4.4, at 141.
56. Id. § 4.4, at 141.
This is the crucial concept for two reasons. First, all of the remedies for responding to waste under the Restatement – foreclosure, an injunction prohibiting future waste or requiring the mortgagor to correct the consequences of his waste, or damages – are dependent on or limited by a finding that the security has been impaired.\footnote{57} Moreover, nothing concerns the mortgagor more acutely than the value of the collateral, other than perhaps the mortgagor’s ability and willingness to continue to pay the underlying debt obligations.

In light of its importance, the Restatement devotes considerable attention to measuring security impairment and proposes innovatively that at least while the mortgage relationship is continuing, the security is impaired only “if the ratio of the mortgage obligation to the real estate’s value is above its scheduled level.”\footnote{58} Unless the mortgage documents specifically forbid some particular use of the property, presumably a mortgagor would not be able to complain about alterations or improvements to the mortgaged property as long as the loan-to-value ratio remains at its scheduled level. If waste occurs under this loan-to-value ratio standard, the mortgagor is entitled to have the mortgagor correct the waste or pay damages in an amount that will restore the scheduled ratio.\footnote{59} In other words, the mortgagor should be able to recover damages to the extent “the waste has deprived the mortgagee of the margin of security for which it bargained when the mortgage was given,”\footnote{60} not just the difference between the value of the property before and after the occurrence of waste or some “maddeningly vague” standard entitling the mortgagee to be restored to a “reasonable” margin of security or that which a “prudent lender” would demand.\footnote{61} Although Professor Merryman may be right that a purely objective market value approach to determining what constitutes waste may be too narrow in the context of life estates where social and altruistic goals might underlie a grantor’s intentions,\footnote{62} surely in the mortgage context, where the purpose of the property relationship is solely economic, a focus on market value measured the way actual market participants view it (through the lens of a scheduled loan-to-value ratio) makes a great deal of sense.

For purposes of this article, though, as innovative as Nelson and Whitman’s definition of impairment of security may be, it is even more important to notice what does not constitute waste under section 4.6 – namely a mortgagor’s failure to repair the real estate when repairs are necessitated by “casualty damage or acts of third parties not the fault of the mortgagor.”\footnote{63} In other

\footnote{57. \textsc{Reformation} \textsc{(Third)} of Prop.: Mortgages \textsc{§} 4.6(b)(1)-(3).} 
\footnote{58. \textit{Id.} \textsc{§} 4.6(c). “If the mortgage relationship has ended,” on the other hand, a mortgagee can establish impairment of security for purposes of claiming waste “if the value of the real estate is less than the sum of the mortgage obligation and the obligations secured by any liens senior to the mortgage.” \textit{Id.}}
\footnote{59. \textit{Id.}}
\footnote{60. \textit{Id.} \textsc{§} 4.6 cmt. f.} 
\footnote{61. \textsc{Nelson} \& \textsc{Whitman}, \textit{supra} \textsc{note} 55, \textsc{§} 4.4, at 143.} 
\footnote{62. \textit{See American Law of Property}, \textsc{supra} \textsc{note} 28, \textsc{§} 20.1.} 
\footnote{63. \textsc{Reformation} \textsc{(Third)} of Prop.: Mortgages \textsc{§} 4.6(a)(2).}
words, under the Restatement "the mortgagor is not responsible for repair or reconstruction of damage caused by natural casualties such as hurricane, earthquake, or lightning, and need not repair the consequence of such casualty loss," even though he may be required to take some measures to prevent further deterioration after the casualty occurs. 64 One practical reason that mortgagors are excused from what would otherwise constitute permissive waste here is that the mortgagee should have, and in most cases will have, hedged the risk of casualty damage by requiring the mortgagor to carry sufficient casualty insurance to cover the cost of repair or restoration of the mortgaged property. 65 Another reason, grounded in altruism or idealism perhaps, is the recognition that when the circumstances and conditions surrounding the mortgage relationship have changed dramatically through no fault of either party, the rules of waste should bend and become more flexible.

These background principles of mortgage waste articulated in section 4.6 lead us to the even more radical innovations suggested by Professors Nelson and Whitman in section 4.7 of the Restatement concerning the application of insurance proceeds. The proposed rule begins in subsection (a) by recognizing that, absent a contrary provision in the mortgage, a mortgagee is generally entitled to receive insurance proceeds (or eminent domain compensation proceeds) "paid on account of loss or damage to the mortgaged real estate, to the extent that the mortgagee's security has been impaired by the loss or damage, as defined in [section] 4.6(c)." 66 This provision is not especially controversial. What comes next in section 4.7(b) is. In this section the Restatement declares that, unless the mortgage provides otherwise, a mortgagee has "a duty" to allow the mortgagor to use the insurance proceeds it receives under subsection (a) resulting from a casualty loss or damage to restore the mortgaged property provided: (1) restoration is "reasonably feasible within the remaining term of the mortgage with the funds received by the mortgagee, together with any additional funds made available by the mortgagor," and (2) "after restoration the real estate's value will equal or exceed its value at the time the mortgage was made." 67 The goal of this rule's rebuttable presumption that insurance proceeds will be used for rebuilding activity is to encourage cooperation between lender and borrower in restoring the real estate, especially given that lenders might be tempted for a variety of reasons (perhaps because interest rates have risen or perhaps out of a legitimate concern about the borrower's ability and willingness to continue to pay the underlying

64. Id. § 4.6 cmt. a (emphasis added).
65. Id. Interestingly, if insurance proceeds are insufficient to restore or repair casualty damage, typical mortgage instruments will still obligate the mortgagor to complete repair or restoration at the risk of violating a waste clause. See Fannie Mae/Freddie Mac Uniform Mortgage - Deed of Trust Covenants - Single Family, in GRANT A. NELSON & DALE A. WHITMAN, REAL ESTATE TRANSFER, FINANCE & DEVELOPMENT: CASES AND MATERIALS app. & 7, at 1209 (7th ed. 2006).
66. RESTATEMENT (THIRD) OF PROP.: MORTGAGES § 4.7(a).
67. Id. § 4.7(b).
Debt) to seize the proceeds as a means of forcing a prepayment of the mortgage.68

Drawing on both the seminal California appellate court opinion in Schoolcraft v. Ross,69 and on the New Jersey Superior Court decision four years later in Starkman v. Sigmund,70 the Restatement's drafters explain that the majority common law rules, which (a) generally permit a mortgagee to apply insurance proceeds to pay down or pay off the outstanding mortgage balance in the absence of any contrary contract language, and (b) recognize a mortgagee’s absolute discretion to choose whether to apply proceeds or allow rebuilding under express election clauses, can have painful consequences for the mortgagor. Without the insurance proceeds available, the mortgagor may only be able to rebuild the mortgaged property by taking out a junior mortgage or by refinancing the existing mortgage, either of which is likely to entail higher interest rates.71 In addition, the residential borrower may well have to pay rent for substitute housing while his home is being repaired, which, in the worst case scenario, could lead him to cease making payments on the underlying note and face the prospect of foreclosure.72 In light of these consequences, the Restatement comments advise that “[i]f restoration is feasible and involves no impairment of the lender’s security, it is unreasonable for the lender to refuse to cooperate.”73 Going even further and drawing more particularly on Schoolcraft, the official comments also advise that even when a mortgage clause expressly gives the mortgagee the right to apply casualty insurance and eminent domain awards to the mortgage debt without imposing any correlative duty to permit restoration, courts might, at least in some instances, be justified in disregarding such a clause as an “unconscionable term” whose “enforcement would violate the mortgagee’s duty of good faith and fair dealing.”74 Here section 4.7 foreshadows the Restatement’s

68. Id. § 4.7(b) cmt. d.
69. 146 Cal. Rptr. 57 (Ct. App. 1978).
71. RESTATEMENT (THIRD) OF PROP.: MORTGAGES § 4.7 cmt. d.
72. This is exactly what happened in Schoolcraft, 146 Cal. Rptr. at 59.
74. RESTATEMENT (THIRD) OF PROP.: MORTGAGES § 4.7 cmt. e (citing RESTATEMENT (SECOND) OF CONTRACTS §§ 205, 208 (1981)). Apparently it was the Schoolcraft decision that first clearly applied the implied covenant of good faith and fair dealing concept to questions of application of insurance proceeds, although an earlier California decision had applied the concept in a case involving application of a condemnation proceeds. Schoolcraft, 146 Cal. Rptr. at 59 (citing Milstein v. Sec. Pac. Nat’l Bank, 103 Cal. Rptr. 16 (1972)).
adoption in section 8.1(d)(3) of a “bad faith” constraint on lender acceleration decisions based on technical or “objective” defaults by the borrower.  

We can see now the challenge that section 4.7 poses to the typical contractarian mortgage law observer. Indeed, Professor Patrick Randolph almost immediately set out to defend the traditional common law majority rules and to critique the Restatement’s calls for application of the implied covenant of good faith and fair dealing. Drawing on decisions upholding the traditional majority rules in this setting, Professor Randolph summarized their classic rationales. First, he noted, requiring a mortgagee to apply insurance proceeds toward rebuilding would essentially force a mortgagee to convert the proceeds into a construction loan and thus force the lender to assume additional risk. Second, applying insurance proceeds to pay down or pay off the outstanding loan balance still benefits the mortgagor by reducing his debt. Third, adoption of a rule requiring proceeds to be used for restoration as long as the security is not impaired would invite disputes and litigation over the sufficiency of the repairs and thus lead to judicial inefficiency. Fourth, the adoption of an implied good faith and fair dealing restoration duty would undermine the certainty desired by the property system generally. And finally, the uncertainty the Restatement rule would inspire might unintentionally cause mortgagees to overreact and draft clauses that automatically apply insurance proceeds to pay off mortgage debt, thus eliminating any possibility of benevolent or mutually beneficial cooperation.  

Given the strength of these arguments for the traditional rules, many observers would probably agree with Professor Randolph – up to a point. In commercial mortgages, for instance, where a mortgage clause expressly provides the lender with the option to apply proceeds or allow restoration, it makes perfect sense to enforce the mortgagee’s right to make this election unburdened by judicial second-guessing. In these cases, the mortgagee is likely to have bargained for the strong discretionary option and thus may have

78. Randolph, supra note 76, at 3.  
79. Id. at 3-4.  
80. Id. at 9, 16-17.  
81. Id. at 9-10.  
82. Id. at 15, 20-21.
given up some other right in exchange. Further, in the case of purchase money mortgages provided by non-institutional lenders, mortgagees might face greater risk exposure after a casualty, rendering them especially reluctant to permit restoration, particularly as they will typically lack the resources and expertise to manage the insurance proceeds in the form of an escrow account and de facto construction loan. But in a typical institutionally originated residential loan, the Restatement's attempt to provide a framework to encourage lender-borrower cooperation toward rebuilding should not only cause considerably less lender distress but also is more likely to match the unexpressed expectations of the parties and, as we shall see later, is likely to serve important community interests. Indeed, Professor Randolph himself acknowledges this difference when he observes that the mortgage industry generally has long adopted this cooperation enhancing model through its uniform Fannie Mae/Freddie Mac mortgage instrument which expressly incorporates an insurance proceeds application model similar to the Restatement's.

Ironically, though, in attempting to criticize the Restatement's endorsement of implied good faith and fair dealing, Professor Randolph actually frames the issue in a way that supports its rebuilding-friendly approach. As he put it, the real question is whether the parties to the mortgage really intended for the mortgagee to have "absolute discretion" to make this choice about application of insurance proceeds or whether they intended for there to be some kind of constrained discretion with the constraint being that the mortgagee should seek, whenever possible, to preserve the long term mortgage relationship. This is fundamentally what the courts in Schoolcraft and Starkman were concerned about—preserving not only the mortgagee's interest in unimpaired security but the mortgagor's property interest in the benefits of a long term loan. In other words, even recognition that a mortgagee has discretion implies that such discretion can be abused in some cases, especially

83. See id. It is noteworthy that in Starkman v. Sigmond, 446 A.2d 1249, 1251-52 (N.J. Super. Ct. Ch. Div. 1982), the mortgagees were the property's former owners who had provided a purchase money mortgage, but significantly the mortgage was silent on the subject of what to with insurance proceeds after a fire.

84. This was the solution suggested by the court in Starkman, 446 A.2d at 1256, and is also recommended by the RESTATMENT (THIRD) OF PROP.: MORTGAGES § 4.7 cmt. d (1997).

85. Randolph, supra note 76, at 20. Here, Randolph notes the advent of the uniform Fannie Mae/Freddie Mac mortgage instrument has largely solved this problem in favor of the residential borrower by providing "virtually from their creation that insurance proceeds can be used to rebuild when the lender’s security interest can be protected." Id. Professors Nelson and Whitman acknowledge the same development. NELSON & WHITMAN, supra note 55, § 4.15, at 167. The exact language used in Fannie Mae/Freddie Mac Uniform Mortgage, can be found in NELSON & WHITMAN, supra note 65, app. & 5, at 1208.

86. Randolph, supra note 76, at 13.

87. Schoolcraft v. Ross, 146 Cal. Rptr. 57, 60 (Ct. App. 1978); Starkman, 446 A.2d at 1254-55.
when the mortgagee really has no legitimate concern that its security would be impaired by permitting rebuilding. Interestingly, Professor Wilson Freyermuth endorses a similar kind of restraint on lender discretion in the mortgage acceleration context. He observes that although a fuzzy good faith rule can impose some costs in terms of loss of predictability for the lender, this uncertainty can produce positive effects as well by leading to more explicit documentation practices (which can then minimize the risk of parties having unexpressed expectations about lender discretion) and, more importantly, by tempering abusive lender acceleration decisions either in marginal cases or when there is no reasonable commercial basis for acceleration. Or, as Professor Randolph puts it in even more general terms, "whenever a party has a choice of performances, the principles of good faith and fair dealing ought to prohibit the party from choosing a performance to the detriment of the other if the alternative performance would serve its own interests equally well."

My reason for taking this lengthy detour into the debate over application of insurance proceeds should be clear by now. We have come full circle in a sense. Professors Nelson and Whitman’s three-step framework for resolving insurance proceed disputes in the Restatement—first, look to the mortgage contract; second, in the absence of an express clause, favor rebuilding but give the mortgagee some room to insist on paying off the debt if restoration is not feasible or would create real risks of security impairment; and third, even when the mortgage contract gives the mortgagee discretion, cabin that discretion with an implied good faith and fair dealing analysis built on the foundation of assuming the parties should try to preserve the existing relationship—sounds a lot like the modern version of the voluntary or ameliorative waste doctrine which is also grounded in notions of reasonableness and mutual accommodation.

Underlying both sets of rules is an emphasis on preserving the property relationship, inducing the possessory interest holder to protect, preserve and invest in the asset while simultaneously coaxing the future interest holder to accommodate the needs of the possessor and any reasonable adaptations to new conditions the possessor may need to make. Perhaps it is fair to say that courts and commentators expect a future interest holder—whether it is a reversioner or remainderman, a landlord or a mortgagee—to behave fairly when circumstances have changed dramatically either because of some external social, economic or environmental development or because of a potentially foreseeable but nevertheless fortuitous event. In short, we expect the

88. Randolph, supra note 76, at 14. The factors that might be considered in making this abuse of discretion finding include: (1) the mortgagor’s reasonable expectations when the mortgage was executed; (2) the amount of mortgagor comprehension at the time of execution; (3) the mortgagor’s ability to obtain substitute financing; (4) the cost of refinancing; and (5) the expectation of a long-term relationship. Id. The last factor was specifically noted by the court in Schoolcraft, 146 Cal. Rptr. at 60.
89. Freyermuth, supra note 73, at 1108-09.
90. Randolph, supra note 76, at 22.
future interest holder to allow the possessory interest holder – the life tenant, tenant for years or mortgagor – to make improvements and alterations in the subject property or to be able to repair or rebuild it, as long as these actions do not cause long term harms or risks to the future interest holder.

D. Four Theories of Waste: Horowitz, Sprankling, Posner and Purdy

Before turning in the last part of this article to two contemporary outbreaks of waste conflict, we should briefly examine what has been said about waste doctrine from a more theoretical perspective. Here the focus is on the noteworthy comments of three scholars and one judge.

First, in his seminal book, *The Transformation of American Law, 1780-1860*, Morton Horowitz examines the crucial period in the early American republic when courts repeatedly rejected the supposedly clear and strict English rule holding that any fundamental alteration of the condition of land by a life tenant or tenant for years constituted waste and replaced it with a more flexible standard based on a detriment to the inheritance. For Horowitz, this mini-transformation in the law of waste illustrates a larger transformation in American law – the transition from an eighteenth century understanding of private law as fixed doctrine to one in which private law adjudication became a creative instrument for promoting social change and economic growth. Horowitz’s analysis thus reminds us that judicial decisions in waste cases, like any other kind of judicial decision, may sometimes exhibit instrumentalist tendencies.

Building on Horowitz’s insights, John Sprankling interprets the same evolution of early nineteenth century waste doctrine as illustrating a more particular tendency of American property law to privilege agricultural development at the expense of wilderness destruction. Specifically, Sprankling claims that the rejection of English common law’s strict rules preventing the conversion of forest land to farm land and limiting a life tenant’s timber cutting to personal consumption uses (estovers), which in England served rational conservation purposes given its wood-dependent economy and wood

91. MORTON J. HOROWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1780-1860, at 54-58 (Stanley N. Katz ed., Harvard Univ. Press 1977). Horowitz claimed that the English law of waste was “relatively clear,” *id.* at 54, a claim that Blackstone and some contemporary scholars would probably contradict. Horowitz also makes the somewhat doubtful claim, based on a small sampling of cases, that “[n]o American court . . . enforced the strict English common law governing waste,” although he admits that some states like New York only modified it. *Id.* at 55.

92. *Id.* at 1-4.

scarcity, served the American instrumentalist goal of converting wilderness into agricultural land.\textsuperscript{94} Sprankling also demonstrates that twentieth century American waste doctrine retains its "anti-wilderness bias" in two ways. First, the doctrine still "encourages the destruction of wilderness lands in pursuit of agricultural expansion."\textsuperscript{95} Second, it "facilitates the conversion of wild forest land unsuited for farming into commercial tree plantations, regardless of the wishes of the preservationist interest holder."\textsuperscript{96} Sprankling's thesis is, I think, incontrovertible as far as it goes. With the curious exception of a few Mississippi cases,\textsuperscript{97} recent timber waste decisions confirm that American courts continue to favor interests of short term possessory estate holders who seek to commence or intensify commercial tree farming activity over preservationist oriented future interest holders' pleas for selective cutting or no cutting at all.\textsuperscript{98}

\textsuperscript{94} Id. at 533-35. Even in cases in which American forest land was not suitable for agriculture if cleared, Sprankling observes, American courts still tended to allow widespread logging by asserting that grantors must have intended for life tenants or tenants for years to be able to continue pre-grant logging activities or must have intended for the tenants to be able to reap the only significant economic value of the land through logging. \textit{Id.} at 536.

\textsuperscript{95} Id. at 570.

\textsuperscript{96} Id. at 570. As Sprankling points out, courts often rationalize these decisions by pointing to some sporadic logging activity of the previous owner, \textit{id.} at 570-71 (citing Merriman v. Moore, 600 S.W.2d 720, 722 (Tenn. 1980)), or by analogizing trees to a crop and then using the "good husbandry standard" to permit logging whenever this enhances the "market value" of forest land. \textit{Id.} at 571 (citing Sutton v. Bennett, 110 S.E.2d 650 (Ga. 1959); Brogdon v. McMillan, 156 S.E.2d 828, 829 (Ga. Ct. App. 1967)).

\textsuperscript{97} See Chapman v. Thornhill, 802 So. 2d 149, 153-56 (Miss. Ct. App. 2001) (holding that a life tenant's rights to harvest timber as estovers does not include right to harvest timber for commercial purposes, even if harvesting would allow tenant to provide himself with essentials for life and increase his standard of living); Twin States Land & Timber Co. v. Chapman, 750 So. 2d 567, 570-71 (Miss. Ct. App. 1999) (allowing life tenant to harvest timber to raise money to pay property taxes, to repair fences and other improvements and for property management and preservation, but not "solely as a commercial enterprise"). In the \textit{Chapman v. Thornhill} decision, the Mississippi court relies heavily on Professor David Thomas' assertions that the law concerning a life tenant's right to cut timber has "made almost a full circle" and that, with the exception of estovers, "[a]lmost everywhere today... timber has become so valuable that the cutting of standing timber by the life tenant is waste." 802 So. 2d at 153 (quoting 2 THOMPSON ON REAL PROPERTY, \textit{supra} note 8, \S 19.08, at 788, 790. The decisions Professor Thomas cites for this claim, however, generally date from the turn of the last century, with the exception of one 1963 decision. 2 THOMPSON ON REAL PROPERTY, \textit{supra} note 8, \S 19.08, at 790 n.418.

\textsuperscript{98} See, e.g., Robinson v. Hunter, 562 S.E.2d 189, 190-91 (Ga. Ct. App. 2002) (holding that life tenant may cut timber and keep all of the proceeds as long as harvesting is in conformity with "good husbandry" and not "solely" for profit); White v. Watts, 812 So. 2d 328, 332 ( Ala. 2001) (permitting life tenant to harvest timber be-
Richard Posner, not surprisingly, uses the subject of waste to illustrate several broad law and economics principles. Posner begins by distinguishing between the parties to a conventional lease and those intertwined in a life estate and reversion or remainder relationship. The former, he assumes, will act as “rational profit-maximizers” and thus will intend that a lessee manage the property as if he were the owner. The life tenant, he assumes, however, will have an incentive to maximize, not “the present value of the entire stream of future earnings obtainable from [the property], but only the present value of the earnings stream obtainable during his expected lifetime.”

The doctrine of waste, according to Posner, developed in the life estate (and not the lease) context precisely to prevent the inefficient, non-profit maximizing tendencies inherent in life estate relationships. Efficiency seeking, Coasian bargaining is less likely to occur in these relationships, he theorizes, because life tenants and remaindermen are typically thrown together by the grants of others and thus locked into bilateral monopolies laden with high transaction costs. According to Posner, the trust performs this same transaction-cost-reducing function even more efficiently than the doctrine of waste by concentrating the value maximizing impulse in the trustee as long as the trustee has proper incentives.

For Posner, as for many others, the trust is thus a more efficient and reliable estate planning tool than the life estate. As noted earlier, this law and economics analysis of waste doctrine has been enormously influential on property law case books which frequently use waste cases as teaching tools to introduce these very same themes.

But is this all there is to waste doctrine? Is it just an example of a high transaction cost, bilateral monopoly situation that should be avoided by choosing a more efficient, externality internalizing property ownership structure? Is it just a way for courts to reconcile the rational profit maximizing
interests of both present and future interest holder? I certainly hope that is not all it can teach us.

Because of this perhaps naïve hope, I am drawn finally to Jedediah Purdy's recent attempt to re-conceptualize waste doctrine in his article The American Transformation of Waste Doctrine: A Pluralist Interpretation. As his title suggests, Purdy approaches the same early nineteenth century period that attracted Horowitz and Sprankling's attention. Yet he reinterprets this transitional moment through a lens which recognizes that property law, like any other social or legal phenomenon, reflects a multitude of values - sometimes contradictory and sometimes mutually reinforcing. Purdy claims his "pluralist account" is more realistic than a myopic "economic account" because it need not assume that (1) humans are always rational, self-interest maximizers, or (2) the pursuit of wealth is always an adequate proxy for self-interest. In contrast, Purdy assumes quite sensibly that people actually care, not just about satisfying their economic self interest, but also about the well-being of others, their own social status, their spiritual standing and lots of other idiosyncratic goals.

Curiously, though, when Purdy actually explains how American courts changed their understanding of voluntary waste in the first several decades of the nineteenth century, he turns to theories concerning the development of default rules in contracts. Here, Purdy suggests that voluntary waste standards can be understood as any of three different kinds of default rules. First, the traditional English common law rule can be understood as an "equilibrium inducing" or "bargaining default rule," a rule whose very strictness might lead parties to bargain expressly over the tenant's power to exploit the reversioner's land. This "equilibrium inducing" and bargain promoting quality, Purdy suggests, is especially noticeable in connection with drastic kinds of exploitation that can fundamentally alter the value of the reversioner's interest - e.g., mineral exploitation - and thus might be expected to and did lead to economically efficient agreements. Alternatively, "the reasonable use" standard that American courts eventually settled on by the end of the transformative period can be understood as a reliable "gap-filling or problem solving default rule," a rule that supplies a term the parties would have chosen had they directed their attention to the issue at the moment of contract or estate formation. This, of course, sounds an awful lot like Richard Pos-

104. Purdy, supra note 7.
105. Id. at 654-55.
106. Id. at 657.
107. Id. at 657-58.
108. Id. at 665 (citing Ian Ayers and Robert Gertner, Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules, 101 YALE L.J. 729 (1992)).
109. Id. at 665. In fact, Purdy observes that American courts uniformly stuck with the strict, English, bargain inducing default rule in the mineral context. Id. at 678-79.
110. Id. at 659 (citing Ian Ayers, Preliminary Thoughts on Optimal Tailoring of Contractual Rules, 3 S. CAL. INTERDISC. L.J. 1, 4-5 (1993); Alan Schwartz, The De-

http://scholarship.law.missouri.edu/mlr/vol72/iss4/8
ner's interpretation of waste doctrine as merely a court's way of asking whether the tenant has acted in a manner that a prudent or rational owner would have acted. And, indeed, Purdy willingly admits this convergence between this second default rule theory and Posner's law and economics account of waste.

Purdy's most intriguing insight comes when he suggests that what American courts were also doing with waste doctrine was rejecting one particular "normative," "status confirming" or "transformative" default rule, a rule that educates the parties about some ideal social structure, and replacing it with another. Here, the transformation was from a rule that emphasizes the life tenant's subordinate position in a feudal hierarchy and simultaneously underscores the reversioner's superior social status to one that illustrates a "Civic Republican" theme in American property law - the "idea of American landholding as a republican enterprise, free of feudal hierarchy."

Although several courts had already begun the process of departing from the "strict" English common law rule and hinting at more flexible waste standards in the first few years of the nineteenth century, for Purdy the key moment in this transformation arrived in one watershed case, *Jackson v. Brownson*. Here, a 3-2 majority of the Supreme Court of New York actually upheld the right of lessors to repossess a 133 acre tract from a tenant for life because the tenant had cut all but 35 acres of the previously wild and uncultivated land. At the same time, though, it adopted a new more flexible "permanent injury to the inheritance" standard as the metric for determining if voluntary waste has occurred. This decision was particularly significant, Purdy explains, for two reasons.

First, the *Jackson* court's adoption of a "permanent injury to the inheritance" standard, and subsequent courts' adoption of an even more finely

---

fault Rule Paradigm and the Limits of Contract Law, 3 S. CAL. INTERDISC. L.J. 389, 390 (1993)).
111. POSNER, supra note 99, § 3.11, at 73.
112. Purdy, supra note 7, at 659-60.
113. Id. at 667 (quoting Schwartz, supra note 102, at 391).
114. Id. at 661. For more on the Civic Republican strain in American property law, see GREGORY ALEXANDER, COMMODITY AND PROPRIETY 21-88 (1997).
115. See, e.g., Ballentine v. Poyner, 3 N.C. 110 (1800) (defining waste as "unnecessary cutting down and disposing of timber, or destruction thereof upon the wood lands, where there is already sufficient cleared land for the widow to cultivate"); Hastings v. Crunkleton, 3 Yeates 261 (Pa. 1801) (calling for an American adaptation of the English common law rule on waste and holding that widow in dower who cut down timber and cleared land did not commit waste as long as a "proper proportion of woodland is preserved for the maintenance of the place"); Ward v. Sheppard, 3 N.C. 283 (1803) (holding that cutting down trees for sale is waste but cutting them down to clear land is permissible); Parks v. Coxe, 3 N.C. 339 (1805) (stating it is waste to cut down timber for sale or to collect it for "lightwood" or to extract tar from it because all of these amount to "permanent[n]t injury").
116. 7 Johns 227 (N.Y. Sup. Ct. 1810).
tuned, though still ambiguous, "appropriate use" conception of waste,\(^{117}\) signals not only a move from a bright line rule to a flexible standard, but also a move from a crystalline, bargain inducing default rule to a welfare maximizing, problem solving default rule.\(^{118}\) We can detect the momentousness of this shift, Purdy notes, in the strident objections of the dissenters in Jackson who defended the strict English common law waste standard. They resisted doctrinal change by pointing out that parties could always covenant for alternative solutions – a Coasian, bargain inducing understanding of the default rule – which they claimed would be easier to administer than an unpredictable hunt for the parties’ intentions or some vague notion of material injury or good husbandry.\(^{119}\)

Second, Purdy claims that Jackson’s social implications were momentous as well. Here, Purdy emphasizes the case’s social setting in the uniquely hierarchical social, political, and legal structure of New York’s Hudson Valley. He contends that the majority’s selection of the material injury standard reflects an attempt to align waste doctrine with “Republican” political, social and cultural values then popular in American society.\(^{120}\) More particularly, drawing on the writing of James Kent, who was also on the New York Supreme Court at the time Jackson was decided and was a silent member of the court’s 3-2 majority, Purdy claims that the majority’s re-conceptualization of waste was broadly supported throughout the emerging American legal community.\(^{121}\) Kent’s silent assent is crucial for Purdy because Kent believed not only in the Republican ideal of a “free-holder” liberated from feudal obligations and subordination, but also in “the formal equality of the marketplace,” the notion that a free holder could easily enter the marketplace and exchange

\(^{117}\) After Jackson, courts increasingly fine tuned the standard for determining waste and moved away from a simplistic market value approach focused on “injury to the inheritance” and often framed the inquiry in terms of whether the improvements and alterations were ones that a “prudent farmer” would make, whether the actions amounted to “appropriate use” or were consistent with local community based or customary standards of “good husbandry.” See, e.g., Owen v. Hyde, 14 Tenn. 334, 339 (1834) (employing “prudent farmer standard”); Shine v. Wilcox, 21 N.C. 631, *2 (1837) (same and adding “usual course of husbandry” to discourse). See generally Purdy, supra note 7, at 673 (commenting on these cases).

\(^{118}\) Purdy raises a number of objections to the purported efficiency of the problem solving default rule approach, particularly his observation that the vagueness of the new American standard might have lulled inattentive parties into “accepting its indeterminate principle rather than bargaining ex ante.” See Purdy, supra note 7, at 677-78.

\(^{119}\) Purdy, supra note 7, at 677 (citing Jackson, 7 Johns at 237 (Spencer, J., dissenting)).

\(^{120}\) Id. at 681-84. By “Republican,” Purdy means a model of society that privileges citizens’ equal rights over the authority of dynastic families, that celebrates personal independence rather than feudal subordination and that assumes ordinary citizens are just as capable of virtue as aristocrats. Id. at 683.

\(^{121}\) Id. at 685.
his labor and land and thus improve his material life. In short, by rejecting a rule that started from the assumption of aristocratic and hierarchical privilege and adopting one that presumes a formal equality of estates, the transformation of the American standard of waste represented in Jackson and its progeny achieved a significant status-conforming goal. Land was no longer a “marker of social hierarchy,” but something that anyone could “acquire, use, and dispose of” in a formally egalitarian marketplace.

The great value of Purdy’s meditation on this brief but important period of American waste law is that it opens our eyes to the symbolic significance of waste doctrine, its social content, and its central relevance to understanding property relationships in which different individuals and institutions claim interests in the same resource across time. His study thus provides a useful bridge from the doctrinally focused and law reform oriented discussions of waste doctrine in the Restatements and some of our great property and real estate treatises to two contemporary outbreaks of conflict about waste doctrine and its close cousin, rules governing application of insurance proceeds in the context of mortgages.

III. TWO TWENTY-FIRST CENTURY WASTE PROBLEMS

Two sets of recent waste cases form the subject of the rest of this article. What ties these cases together is the role that radically changing conditions can play in transforming fairly straightforward waste problems into extremely controversial waste conflicts. The pressure of these suddenly changed circumstances can lead courts and legislatures to craft new rules or at least to reexamine basic assumptions about waste. In the first instance, we see courts and eventually a legislature struggle to craft rules and procedures to respond to the harmful effects that oil and gas exploration and production can have on land and the environment. In the second, we see how courts, lenders and government have responded to the crises that the 2005 hurricane season created for thousands of homeowner-mortgagors on the Gulf Coast.

A. The Legacy Litigation Phenomenon: Restoration of Premises under Mineral Leases

The first contemporary waste problem arises primarily out of a special kind of property relationship – that between a landowner (or mineral serv-
and a mineral lessee under Louisiana law. Before plunging into the details, a few words about a Louisiana mineral lease are in order.

1. The Louisiana Mineral Lease and the Duty to Restore

Just as in the rest of the United States, a Louisiana mineral lease is essentially a contract between a producer-lessee and a landowner or mineral servitude owner which grants the lessee the right to explore for and produce minerals. It is essentially a bilateral contract under which the specific rights and obligations of the parties are defined by its contractual provisions and, when those provisions are silent, by the default rules of the Louisiana Mineral Code and the Louisiana Civil Code. Despite this essentially contractual nature, when it comes to protecting a mineral lease interest against third parties under the laws of public registry and for other purposes (e.g., conflicts of laws, prescription of non-use, access rights, after-acquired-title doctrine), Louisiana law treats mineral leases as “real rights” and as “incorporal immovable” – i.e., as real property.

During the existence of the lease, the lessee, while not held to a fiduciary standard of care with respect to the lessor, “is bound to perform the contract in good faith and to develop and operate the property leased as a reasonably prudent operator for the mutual benefit of himself and his lessor.”

Given the vague and undefined nature of this “reasonably prudent operator standard,” the Mineral Code allows the parties to “stipulate what shall constitute reasonably prudent conduct on the part of the lessee.” The general problem that arises then is to determine exactly what the precise scope of this “reasonably prudent operator” standard is when a contract is silent or its stipulations are unclear. The more particular problem that has arisen in recent years is whether a mineral lessee has a duty to restore the surface of the land to its pre-lease condition at the termination of the mineral lease and, if such a duty exists, whether there are economic limits to the liability of a mineral lessee.

125. A mineral servitude owner is someone who owns the “exclusive right to explore and develop either oil and gas or solid minerals” when that interest is “separated from the fee title.” John McCollam, A Primer for the Practice of Mineral Law under the Louisiana Mineral Code, 50 Tul. L. Rev. 729, 740 (1976). See also LA. REV. STAT. ANN. § 31:21 (2000) (defining a mineral servitude as “the right of enjoyment of land belonging to another for the purpose of exploring for and producing minerals and reducing them to possession and ownership”).

126. McCollam, supra note 124, at 782. See also LA. REV. STAT. ANN. § 31:114 (defining a mineral lease as “a contract by which the lessee is granted the right to explore for and produce minerals”).

127. McCollam, supra note 124, at 783.

128. Id. at 785-93. See also LA. REV. STAT. ANN. §§ 31:16, 31:18.

129. LA. REV. STAT. ANN. §§ 31:122 (emphasis added).

130. Id.
lessee who breaches this duty. It is a problem, in other words, of defining what constitutes waste and the appropriate remedies for waste.

Prior to the key decisions that emerged in the last few years, Louisiana law was surprisingly vague on the subject as courts reached conflicting conclusions in a number of old oilfield waste cases. Several intermediate appellate decisions had recognized that a lessee has a general duty to restore the surface of the land if the lease is silent on the subject.\textsuperscript{131} A number of decisions, however, including those recognizing the general duty to restore, had also held that a reasonableness inquiry would limit restoration damages as a lessee is only responsible for damages caused by \textit{negligent} or \textit{unreasonable} exploitation and production activities, not damage caused by \textit{reasonable} and \textit{necessary} exercise of its rights.\textsuperscript{132} The oldest decision, predating the Mineral Code and authored by an eminent Louisiana Supreme Court justice, Oliver Provosty, noted that, though a mineral lessee might be obliged to act as a "good administrator," he was not like an ordinary lessee.\textsuperscript{133} In fact, the court was distinctly unsympathetic to the landowner's claim for restoration damages, analogizing the landowner's damaged fences and standing timber to obstructions and annoyances to the mineral lessee rather than valuable assets that deserved protection.\textsuperscript{134} Finally, although the drafters of the Mineral Code failed to expressly include a lessee restoration obligation in its provisions, they nevertheless observed in their official comments that a duty to

\begin{itemize}
\item \textsuperscript{131} See Edwards v. Jeems Bayou Prod. Co., 507 So. 2d 11, 13 (La. Ct. App. 1987) ("A mineral lessee has the obligation to maintain or restore the leased premises as near as is practical to its original condition, subject to the lessee's rightful use thereof, and where the lessee has damaged the land it is his duty to appropriately remedy the condition brought on by his use of the lease."); Broussard v. Waterbury, 346 So. 2d 1342, 1344 (La. Ct. App. 1977) (holding that mineral lessee has "an obligation to reasonably restore the land to the same state as before the drilling and production"); Smith v. Shuster, 66 So. 2d 430, 431-32 (La. Ct. App. 1953) (observing that mineral lessee should "maintain and restore the premises in the condition he found them subject to his rightful use, and where he has damaged the land it is his duty to appropriately remedy the condition brought on by his use of the lease").
\item \textsuperscript{132} See Edwards, 507 So. 2d at 13 (stating that a lessee's liability for damages is subject to a reasonableness inquiry because a "mineral lessee has the right to conduct its operation in accordance with the mineral lease and the landowner has no right to recover damages for diminished use of his land arising out of reasonable and necessary exercise of the lessee's rights under the mineral lease"); Ashby v. IMC Exploration Co., 496 So. 2d 1334, 1337 (La. Ct. App. 1986) (holding that mineral lessee can be liable for unreasonable use of the land but that negligence per se is \textit{not} a prerequisite to recovering damages); Broussard, 346 So. 2d at 1344 (agreeing that a standard of reasonableness should be used in assessing restoration damages); Rohner v. Austral Oil Exploration Co., 104 So. 2d 253, 255 (La. Ct. App. 1958) (holding that mineral lessee is not liable for damages to the lessor's property resulting from "reasonable and necessary use").
\item \textsuperscript{133} Wemple v. Pasadena Petroleum Co., 85 So. 230, 231 (1920).
\item \textsuperscript{134} Id.
\end{itemize}
restore the surface existed under the basic obligations principles of the Louisiana Civil Code if a mineral lease was silent on the issue. At the same time, however, they asserted that some kind of "economic balancing process" should occur to limit the extent of a lessee's restoration liability, citing one of the decisions articulating a vague reasonableness standard for measuring the duty to restore. Perhaps most important, though, all of these prior judicial decisions had been relatively uneventful cases in which aggrieved landowners had sought restoration damages ranging anywhere from a few hundred to a few thousand dollars. In other words, the stakes were small and the judicial attention devoted to the subject was commensurately limited. This changed in the beginning of the twenty-first century.

2. The Corbello Bombshell

The current controversy erupted with a lawsuit entitled Corbello v. Iowa Production, whose ultimate resolution shook the Louisiana legal community like few others in recent memory. The case began when the owners of a 320 acre tract of land in Calcasieu Parish filed suit against several defendants, including Shell Oil Corporation. In 1929, the plaintiffs' ancestors had granted Shell a mineral lease on their entire 320 acre tract. Shell conducted operations under this lease until 1985 when it transferred the lease to another production and exploration company. In 1961, Shell also obtained a 30 year surface lease on 120 of the 320 acres subject to the mineral lease. Pursuant to this surface lease, Shell built and operated a five acre oil terminal. In 1991, when the surface lease expired, the landowners told Shell that it had breached the surface lease by disposing of damaging saltwater produced by other operators on the property and by failing to maintain the property as provided in the lease. The parties negotiated for a while, but in 1992 the landowners brought suit against Shell and another company (which subsequently settled) seeking to recover damages for Shell's continued presence on the property after termination of the surface lease, for unauthorized disposal of saltwater produced by other operators, and for the generally poor condition of the

135. LA. REV. STAT. ANN. § 31:122 cmt.
136. Id. (citing Rohner, 104 So. 2d at 255).
137. See, e.g., Edwards, 507 So. 2d at 13-14 (reducing trial court damage award from $4,375 to $2,175 based on finding that landowner was not entitled to damages for loss of hay he might have grown on damaged agricultural land due to unreasonable use); Broussard, 346 So. 2d at 1344 (affirming $9,000 restoration damage award); Smith v. Shuster, 66 So. 2d 430, 432 (La. Ct. App. 1953) (affirming $170 damage award); Rohner, 104 So. 2d at 254-56 (affirming $900 in damages for loss of corn and watermelon crop, the latter of which was destroyed in part by the lessee's employees' actual consumption of the melons, but rejecting a claim for $1000 in damages due to loss of productivity of four acres of farm land because the lessee's operations were not unreasonable).
leased premises upon termination of the surface lease, including the alleged contamination of an underground aquifer that provided drinking water for the nearby city of Lake Charles. In essence, the plaintiffs were contending that Shell had committed what common law lawyers might call voluntary waste.

A key question, of course, was whether the parties had anticipated this kind of problem at the time they executed their leases. Not surprisingly, the evidence was ambiguous. On one hand, the parties did at least dimly recognize that the lessee would have some kind of duty to restore the premises because they specifically covenanted in the 1961 surface lease that upon the lease's termination Shell would "reasonably restore the premises as nearly as possible to their present condition." What might the parties have intended with this language? At the time the lease was confected, the Louisiana Mineral Code had not yet been drafted, and, as we have seen, the judicial decisions addressing a mineral lessee's duty to restore were conflicting. At that time, one decision had clearly recognized that the mineral lessee had a duty to restore the land's surface, even if the lease was silent on this subject; but another had imposed a reasonableness limitation on the extent of those damages. Perhaps all that can be said with any certainty is that the parties recognized that Shell or its assignees might have to do some restoration work at the end of lease but that this duty would be subject to some limitation.

In 1992, when the lawyers for the plaintiff landowners filed their petition, they made a bold, and in hindsight, brilliant strategic decision. Rather than frame their action as one sounding largely in tort, they framed their principal demands in contract, relying heavily on the express restoration covenant in the surface lease. After a two-and-a-half week trial, a jury awarded the landowners a stunning amount of monetary damages: $927,000 for Shell's failure to vacate the premises (which the trial court reduced to $32,000); $16,679,000 for Shell's illegal disposal of saltwater produced by other operators; and, $33,000,000 to restore the leased premises to its 1961 condition under the terms of the surface lease — $28,000,000 of which was for the threatened contamination of the aquifer. After a stop at the Louisiana Third Circuit Court of Appeal, which increased the plaintiffs' attorney fee

139. Id. at 691, 697.
140. The waste was voluntary rather than permissive because the alleged damages resulted primarily from Shell’s affirmative acts rather than failures to repair existing structures or pay carrying costs. STOEBUCK & WHITMAN, supra note 1, §§ 4.2-4.3.
141. Corbello, 850 So. 2d at 694 (emphasis added).
145. Corbello, 850 So. 2d at 694.
146. Id. at 691-92, 697.
award from $695,000 to $4,000,000, reversed the trial court’s remittitur on trespass/holdover damages, opened the specter of a punitive damages award, and affirmed the other damage awards, the case reached the Louisiana Supreme Court.

In its lengthy opinion, the supreme court remanded the case to the trial court to recalculate both the salt water disposal and trespass damage awards in ways that were sure to substantially reduce their size, held that punitive damages were not available, but, in the portion that stunned the Louisiana legal community, affirmed the $33,000,000 restoration damage award and the $4,000,000 attorney fee award. What shocked observers most was not just the absolute size of the restoration damage award, or even the fact that the court allowed $28 million in damages for monitoring and remediating the seriously threatened, but not yet conclusively proven, damage to the public aquifer, but the fact that the estimated market value of the land itself, even if fully restored, was only $108,000. Almost as shocking was the court’s ruling that plaintiff landowners were not required to use the damage award to remediate the property, even though a large part of the damage award was designed to compensate for the threatened public injury to the aquifer. The court justified this part of its ruling by observing that plaintiffs who recover damages are often not required to use monetary damages for a specified purpose and that absent some express legislative directive it was not prepared to impose such a restriction on the plaintiffs here despite the public nature of a significant part of the injury for which they obtained compensation.

In the crucial portion of its opinion affirming the restoration damage award, the court held that a damage award for failure to restore the leased premises to its pre-lease condition need not be “tethered to the market value of the property” nor subject to a rational or reasonable relationship limit when the plaintiff brings a claim based in contract rather than tort. In its key doctrinal move, the court distinguished a line of cases that had restrained

147. Id. at 692. See also Corbello v. Iowa Prod., 806 So. 2d 32, 53 (La. Ct. App. 2001).
148. Corbello, 850 So. 2d at 703-07, 708-09.
149. Id. at 707-08.
150. Id. at 701.
151. Id. at 710-11.
152. Id. at 697-98.
153. Id. at 699. To be fair to the plaintiffs, the facts indicated that they did intend to clean up the land. In fact, their family had owned the land since 1915. Id. at 700.
154. Id. at 699. The court’s examples of plaintiffs who are not required to use damages for a specified purpose include a business that recovers for damage to a building but is not required to use the damage award to repair the building and a personal injury plaintiff who is not required to use a lost income award to buy an annuity. Id. Of course, these examples only involve public injury in a very indirect way, unlike the damage to the public aquifer in this case.
155. Id. at 691-93.
property damage awards arising in tort, but not in contract, reasoning that “the contractual terms of a contract, which convey the intentions of the parties, overrule any policy considerations behind such a rule limiting damages in tort cases.” In addition, the court rejected Shell’s argument that the parties had “bargained for a restoration obligation limited by ‘reasonableness,’” in particular one that would call for an “economic balancing process” to take place. In effect, the court seemed to be saying that a sophisticated oil and gas company like Shell could have negotiated for and inserted a market value or economic balancing limitation on the restoration obligation to which it expressly agreed under the contract and that its failure to do so gave the jury a chance to determine the extent of “reasonable” restoration damages in the event of a breach. Finally, the court offered its own broad policy rationale for its holding (despite its earlier suggestion that the parties’ contractual choice negated any policy considerations underlying the tort damage cases), explaining that a market value limitation would in effect give oil and gas lessees like Shell a license to perform their operations in any manner they want, with “indifference as to the aftermath.” The court was afraid, in other words, that if it imposed a market value limitation on property damages, a breaching tenant like Shell would not have sufficient incentives to internalize the externalities that its conduct was anticipated to produce.

3. Putting *Corbello* in Context

What can we say about this decision? Readers familiar with classic decisions in the contracts cannon such as *Jacobs & Young v. Kent*, *Groves v. John Wunder Co.* and *Peeveyhouse v. Garland Coal & Mining Co.* will

156. *Id.* at 695. The court in this way distinguished its prior ruling in *Roman Catholic Church of the Archdiocese of New Orleans v. Louisiana Gas Service Co.*, in which it had held that, although a plaintiff who has sustained property damage generally can elect between restoration costs or the difference in market value before and after the harm, damages are only measured by market value difference when restoration costs are “disproportionate to the value of the property or economically wasteful,” or there is a “reason personal to the owner for restoring the original condition” or “there is a reason to believe that the plaintiff will, in fact, make the repairs.” 618 So. 2d 874, 879-80 (La. 1993).

157. *Corbello*, 850 So. 2d at 692-93.

158. *Id.* at 693-95.

159. *Id.* at 695.

160. 129 N.E. 889, 891 (N.Y. 1921) (holding that owner of residence is entitled to restoration damages for breach of construction contract by contractor who used different kind of pipe than that called for in the contract unless the cost to restore is disproportionate to the benefit achieved).

161. 286 N.W. 235, 238 (Minn. 1939) (holding that owner is entitled to damages equal to reasonable cost of re-grading property as called for in contract permitting removal of sand and gravel from owner’s land and not just difference in value resulting defendant’s deliberate and willful breach).
see this as just another hard case. They may see it as illustrating how common sense concerns about economic waste justify the Restatement (Second) of Contracts rule that property damages resulting from contractual breach should generally be limited to a diminution in market value whenever restoration damages are "clearly disproportionate to the probable loss in value." Some property law professors might frame the case in terms of nuisance. Drawing on the property rule-liability rule paradigm and Boomer v. Atlantic Cement Co., they would ask whether a liability rule entitlement protection device (limiting the landowner's remedy to actual market value damages) should be used rather than what seems much closer to a property rule solution (restoration of the property to its pre-lease condition) when the latter threatens to cause undeniable economic waste. Finally, if we look at the problem as a standard waste case, perhaps arising in the context of a life estate or a conventional lease, we might be tempted to say, as Professors Stoebuck and Whitman point out, that this decision simply deviates from the general rule that "the appropriate measure of damages [for the commission of waste] is generally the diminution in market value of the property or the cost of restoring the property to its former condition, whichever is less." But what can we say about it now, informed as we are about the shifting debates that have taken place over proper waste standards during the last eighty years?

First, as noted earlier, we must admit that the parties' use of the qualifier "reasonable" in the original lease restoration clause probably implied some intent to limit the amount of restoration charges that could be assessed at termination of the lease. At the same time, we can also understand how the court might have feared that adoption of an "economic balancing" or market value limitation on oilfield restoration damages might be read by lessees as an invitation to engage in wantonly negligent operating activities that could impose major externalities on the lessors, neighboring landowners and the pub-

162. 382 P.2d 109, 114 (Okla. 1962) (limiting landowners damages against strip mining lessee who breached contractual restoration obligation to diminution in property's market value where economic benefit to be gained by lessor from full performance is grossly disproportionate to cost to complete).


165. STOEBUCK & WHITMAN, supra note 1, § 4.4, at 161 (emphasis added). Professors Stoebuck and Whitman also acknowledge that courts sometimes disagree "as to which of these two measures is preferable." Id.

166. See supra notes 141-144 and accompanying text.
lic at large.\textsuperscript{167} And there is some truth to the notion that a sophisticated party like Shell could have bargained for a more explicit limitation on its restoration obligations had that been its contracting goal.

But recalling Jedediah Purdy’s analysis, we should also consider whether the court saw itself here as establishing a new “bargain inducing” or “equilibrium inducing” interpretative default rule, as opposed to a problem solving, welfare maximizing one.\textsuperscript{168} In other words, the court might have been saying that oil and gas lessees like Shell who agree to perform some kind of restoration work on the surface of the leased premises must now ask for clear limits on their liability for committing waste and thus signal to landowners the likelihood that the damage to their property could be extensive. Perhaps the court was creating a new “normative,” “status confirming” or “transformative” default rule, one that puts landowners in a position of equality with oil and gas producers and lessees rather than in a subordinate position in which they have to make explicit demands for restoration of the surface of their land and give up other rights in order to obtain a firm and meaningfully enforceable restoration obligation.\textsuperscript{169}

Finally, to some commentators the most troubling aspect of the court’s ruling in Corbello was its holding that the restoration damages did not, in fact, have to be used for actual restoration but could be retained by the plaintiff landowners who might only superficially restore the land or not perform any restoration work at all.\textsuperscript{170} This specter, as we shall see, was a significant impetus for the legislative response that eventually followed the Corbello decision. But before we address this legislative response, we should also consider two more recent decisions involving damage to coastal wetlands in Louisiana resulting from oil and gas development.

\textsuperscript{167} Corbello v. Iowa Prod., 850 So. 2d 686, 695 (La. 2003).
\textsuperscript{168} Purdy, supra note 7, at 665.
\textsuperscript{170} Balhoff, supra note 163, at 289, 300-01 (arguing for a specific performance remedy or deferral to an administrative agency supervised clean up solution as opposed to the “windfall” approach of the court in Corbello); Loyd J. Bourgeois, Private Actions Seeking Remediation or Restoration Damages: Who Ensures the Cleanup Actually Occurs, 17 TUL. ENV. L. J. 355, 362-63, 366-71 (2004) (complaining about risk of “windfall” awards and endorsing administrative agency preemption of oilfield contamination claims as under Oklahoma and Mississippi statutes). See also Chevron, U.S.A., Inc. v. Smith, 844 So. 2d 1145, 1146 (Miss. 2003) (holding that contamination damage to property previously subject to an oil and gas lease must first be addressed by the Mississippi Oil and Gas Board before any private damage claims can be asserted).
4. The Louisiana Supreme Court's Post-Corbello Retreat

In *Terrebonne School Board v. Castex*, the Louisiana Supreme Court took a notable step back from its dramatic pro-landowner position in *Corbello*. Here, the court held that even though Article 122 of the Louisiana Mineral Code requires a mineral lessee to act as "a reasonably prudent operator," the Mineral Code does not impose an implied duty to restore the surface of land to its pre-lease condition unless damage is caused by "unreasonable or negligent operations." In this case, the alleged harm consisted of the actual loss of 27 acres of freshwater floatant marsh caused by the dredging of canals to facilitate the mineral lessee's exploration and drilling activities. The problem for the plaintiff landowner was that the 1963 lease (based on a 1948 form lease promulgated by the state Mineral Board) specifically authorized the lessee to dredge canals to facilitate its activities but did not contain any restoration clause at all. In 2001 (two years before the final *Corbello* decision), the trial court found two defendants (assignees from the original lessee) solidarily liable for $1.1 million in restoration damages but ordered the defendants to deposit the funds into the registry of the court, appointed a special master to oversee development and implementation of a restoration plan, and ordered that if any funds were left over they should be returned to the defendant. The intermediate appellate court affirmed the damage award, holding that Article 122 did imply a duty to restore the surface of the land, but vacated the special master procedure and simply ordered the defendants to specifically perform their restoration obligation according to the trial court's methodology without regard to cost.

In reversing the lower court decisions, the supreme court justified its holding that no implied restoration duty existed under Louisiana law on several grounds. First, even though Mineral Code Article 122 expressly requires a mineral lessee to "perform the contract in good faith" and "to develop and operate the property leased as a reasonably prudent operator for the mutual benefit of himself and his lessor," and even though the Code’s official comments state that an implied surface restoration duty can be inferred from the Louisiana Civil Code articles on lessee obligations, the court held that the Mineral Code itself did not expressly adopt such a duty. Indeed, it pointed out that its own prior decisions never recognized such a duty and that

171. 893 So. 2d 789 (La. 2005).
172. Id. at 801.
173. Id. at 792-93.
174. Id. at 794. Ironically, the original lessee in this case was also Shell, the same principal defendant as in *Corbello*. Id.
175. Id. at 794-95. See also *Terrebonne Parish School Bd. v. Castex Energy, Inc.*, 878 So. 2d 522, 534 (La. Ct. App. 2004).
177. *Castex*, 893 So. 2d at 797 (discussing LA. REV. STAT. ANN. § 31:122 cmt.).
178. Id. at 801.
intermediate appellate court decisions only impose such an obligation when a lessor shows that surface injury is caused by negligent or unreasonable operation of the lease.179 Moreover, the court also observed that the basic restoration obligation imposed on a generic lessee under the Louisiana Civil Code does not require return of the property in an “unchanged condition” but allows for necessary “wear and tear.”180 This last insight was crucial for the court because when it looked to the lease and saw that the lessee had been granted authority to dredge the canals, this suggested an implied consent on the lessor’s part to the consequential wear and tear that dredging would entail.181 In other words, the specific contractual grant of dredging authority and the lack of a correlative duty to restore in the lease, coupled with the absence of any evidence that the lessee had operated the lease (or dredged the canals) in an unusual or unreasonable manner,182 enabled the court to conclude that no restoration damages were owed. Thus, the precise holding of the case, if properly understood, is a narrow one: “where the mineral lease expressly grants the lessee the right to alter the surface” and “is silent regarding restoration,” then “article 122 only imposes a duty to restore the surface to its original condition where there is evidence of unreasonable or excessive use.”183 The significance of the holding lies, however, in the fact that perhaps many leases that still govern active drilling, exploration and canal dredging activity in Louisiana may also, like the form lease at issue in this case, contain gaps with respect to lessee restoration obligations.

Considering the Casteex decision in the broader waste framework, we see a very different kind of default rule emerging. Just as in Corbello, the court adopts a relatively harsh bargain inducing or equilibrium inducing, rather than a welfare maximizing or problem solving default rule. But now the rule is based on the apparent assumption that a landowner has the initial responsibility to demand and negotiate for some acknowledgement of a lessee’s restoration responsibility if he wants to assure that the mineral lessee will restore the surface. Once that happens, however, under Corbello it is the lessee who is assumed to have the burden of then demanding and bargaining for a mone-

179. Id. at 797-99. Interestingly, the court also observed that Article 22 of the Mineral Code does expressly require a mineral servitude holder (as opposed to a lessee) “insofar as practicable, to restore the surface to its original condition at the earliest reasonable time” and that this apparent differentiation between obligations imposed on lessees and servitude holders also supports its holding. Id. at 801 n.11.
180. Id. at 800 (citing LA. CIV. CODE ANN. arts. 2719-2720 (2005)).
181. Id.
182. Id. at 801.
183. Id. at 792. Unfortunately, the court later broadened its statement of its holding by leaving out any reference to the crucial grant of dredging authority when it stated “we hold that, in the absence of an express lease provision, Mineral Code article 122 does not impose an implied duty to restore the surface to its original, pre-lease condition absent proof that the lessee has exercised his rights under the lease unreasonably or excessively.” Id. at 801.
tary or other kind of limit on the extent of that restoration responsibility. Is this a realistic way of approaching the problem of waste in the context of a mineral lease? Is it possible that the court got these two cases backwards? Might it have been more consistent with prior decisions and the understanding of the drafters of the Mineral Code to hold that some basic implied restoration duty exists if a mineral lease is silent but to impose some realistic and meaningful limits on the extent of that duty? After all, the typical landowner and mineral lessee probably assume that the lessee will have some minimal obligation to restore the surface of the land to some semblance of its pre-lease condition. But extremely extensive restoration that might be associated with unanticipated environmental contamination or wetland loss whose remediation costs could swamp the value of the land itself was probably, at least before Corbello and Castex, not commonly contemplated by either party.

Perhaps what is missing here is a third case, or at least recognition by the courts of a third possibility. This would be a case in which a mineral lessee causes substantial surface damage to the leased premises but does so by dredging canals, disposing of salt water, or otherwise altering the land in a manner that is not inconsistent with standard and customary operating procedures, and yet the mineral lease neither authorizes the particular harm inducing activity nor contains a restoration clause. Unlike the Castex or Corbello cases (neither of which were true default cases because in each there was some contractual language that either implied a duty to restore or implied a duty not to restore the specifically authorized alteration of the surface), in this case an ultimate default rule would be needed because the parties would have neither specifically authorized any particular kind of surface altering activity nor indicated an intent for the lessee to restore the surface. In this circumstance, a court or the legislature would be wise to impose some basic restoration duty, perhaps limited in scope by some form of economic balancing or at least by a requirement that damage awards be used to restore the premises.

5. An Alternative Approach: The Servitude Model

Perhaps we can find a model for what this default restoration duty might look like in a third important, but much less frequently commented upon coastal wetland restoration decision that actually preceded both Corbello and Castex. In this case, Terrebonne Parish School Board v. Columbia Gulf Transmission, the Fifth Circuit Court of Appeals held that the owner of a pipeline servitude has a duty, in the absence of any contrary language in the servitude agreement, not to aggravate the condition of the servient estate by allowing a pipeline canal dredged under the authority of the servitude agreement to widen beyond the specified width of the canal or of the servitude itself.184 Here, there were three crucial legs to the court’s decision. First, the court carefully parsed the servitude agreements that gave the defendant pipe-

184. 290 F.3d 303, 315-17 (5th Cir. 2002).
line companies the right to dredge canals and found that they did not release the servitude holders from damages arising from failure to maintain the canals or their banks.  

Second, it found that the servitude agreements did not evidence any intent to anticipate erosion damage or assign liability for such damage to either the dominant or servient estate.  

Third, the court pointed to the clear default rule in the Louisiana Civil Code governing the relationship between a dominant and servient estate pursuant to a predial servitude—namely that the dominant estate must not "aggravate" the condition of the servient estate. This last point echoes the Mineral Code which expressly imposes on a mineral servitude owner, as opposed to a mineral lessee, an obligation to restore the surface of the land "to its original condition at the earliest reasonable time."

In this decision the Fifth Circuit in effect establishes yet another waste default rule in the context of oil and gas exploration, but this time the rule imposes on the dominant estate owner the obligation of negotiating for clear waivers of liability for the consequences of altering or eroding fragile coastal marshlands. Because so many thousands of miles of pipeline canals have already been dug and caused extensive erosion of Louisiana’s coastal wetlands, however, the real import of this decision may be in its ex post allocation of repair liability if other governing pipeline servitude agreements are determined to be similarly vague.

6. The Legislature Reacts

In the end, the degree of uncertainty created by the Corbello decision was so great that the oil and gas industry lobbied for and passed two different statutes designed to reign in the flood of so called “legacy litigation” that followed in its wake. The first, which was enacted in 2003, applies to

185. Id. at 311-12 (finding that standard form release executed in conjunction with the pipeline servitude only released the defendants from liability for damages arising from construction of the pipelines).
186. Id. 312-15.
187. Id. at 316. See LA. CIV. CODE ANN. art. 743 (1980) (“Rights that are necessary for the use of a servitude are required at the time the servitude is established. They are to be exercised in a way least inconvenient for the servient estate.”).
190. Among the reported “legacy litigation” decisions that relied on or extended Corbello, the most significant are Hazelwood Farm, Inc. v. Liberty Oil & Gas Corp., 844 So. 2d 380, 387-89 (La. Ct. App. 2003) (relying on Corbello to affirm a $2 million jury verdict for damage resulting from mineral lessee’s construction of brine pit, though land itself was only worth $304,000 and holding that landowner could recover
damage claims related to contamination or pollution of ground water and requires a plaintiff to notify two state agencies of the claims and give these agencies an opportunity to intervene in the suit.\textsuperscript{191} Once contamination is determined to exist, the statute then requires the court to oversee the development of an evaluation and remediation plan which is funded by the responsible parties’ deposit of the funds necessary to pay for the plan into the registry of the court.\textsuperscript{192} It then mandates return of any excess funds to the defendants upon the complete execution of the plan.\textsuperscript{193} Because this statute was fairly easily avoided by landowner lawyers who simply dropped “ground water” claims from their petitions, pressure continued to build for an even broader legislative solution.

In 2006, the devastation of New Orleans and much of the Louisiana Gulf Coast by Hurricanes Katrina and Rita created an even stronger climate for legislative response. Many analysts had pointed out that one reason coastal communities were so vulnerable to the hurricane’s powerful storm surge was that the state’s coastal wetland had been disappearing at an alarming rate. One of the most significant, if not the most significant, cause of this wetland loss, according to many scientists and observers, is the destruction directly caused by oil and gas exploration and drilling activities – particularly from the dredging of canals for access to drilling sites and for pipelines to pump the oil and gas away.\textsuperscript{194} In response to a widespread desire to prevent further wetland loss, to facilitate wetland recovery, and to solve the continuing uncertainty created by \textit{Corbello} and its progeny, the Louisiana legislature passed another legacy litigation reform act.\textsuperscript{195} The second act, however, applies much more broadly than the first by covering claims for any “environmental damage,” including, but not limited to, damage to “soil, surface water, ground water or sediment,” and resulting from activities associated with “oil-field sites or exploration and production sites.”\textsuperscript{196}

\textsuperscript{191} LA. REV. STAT. ANN. § 30:2015.1(B).
\textsuperscript{192} LA. REV. STAT. ANN. §§ 30:2015.1(C)(1), (C)(3), (E)(1).
\textsuperscript{193} Id. § 30:2015.1(E)(4).
\textsuperscript{195} LA. REV. STAT. ANN. §§ 30:29, 30:29.1.
\textsuperscript{196} \textit{See id. §§ 30:29(A), (I)(1).
The 2006 Act also moves even further toward an administrative law model as a solution to the oil field waste problem than the 2003 Act. The 2006 Act establishes a remedial scheme requiring plaintiffs to notify state agencies (the Commissioner of Conservation and the Attorney General) of covered suits and provides these agencies with an opportunity to intervene in any covered suit. It requires the development of a remediation plan once a determination of environmental damage has occurred and requires review of the plan by the Louisiana Department of Natural Resources (LDNR). It also calls for a public hearing and comment period, requires approval of the remediation plan by the LDNR based on application of uniform, scientifically derived standards for contamination and remediation, requires court adoption of the plan and funding of the plan through the same method of depositing monies into the registry of the court as in the 2003 Act, and gives the court authority to supervise the expenditure of those funds on required remediation activities, with excess funds to be returned to the depositing defendant. Finally, it provides for expedited, de novo appellate review of the court's plan. In other words, the Louisiana legislature decided that a methodical, costly, but theoretically more uniform administrative law process for resolving oil field waste disputes was preferable to the uncertainty of the ex post, trial lawyer influenced, decision making of judges and juries trying to pin down the reasonableness of restoration duties and damages on a case-by-case basis.

This brief but intense journey from Corbello to the still uncharted waters of Louisiana's hybrid judicial and administrative oilfield damage remediation scheme demonstrates how two new conditions transformed the legal system's response to what would, in another era, have been a relatively routine waste problem. The first new condition was the emergence of a well financed, disciplined and aggressive plaintiffs' bar willing to invest substantial resources and expertise in litigating oilfield waste cases because of the potential for huge attorney fee awards. The second was the environmental crisis created by contamination and coastal wetland loss associated with oil and gas exploration and drilling. As a result of these new circumstances, Louisiana abandoned its previously vague default rules of waste in the context of mineral leases and saw its supreme court issue rulings that oscillated sharply depending on the extent of the parties' ex ante contractual stipulations for restoration obligations. In one decision the court imposed a significant burden on mineral lessees who contractually obligated themselves to "reasonably restore" oilfield waste and contamination, but then turned around in another case

197. Id. §§ 30:29(B)(1)-(2).
198. Id. § 30:29(C)(1).
199. Id. §§ 30:29(C)(2)-(3), (I)(3).
200. Id. §§ 30:29(C)(5)-(6)(a), (D).
201. Id. § 30:29(C)(6)(b).
and relieved mineral lessees of any obligation to restore a lessor’s land to pre-lease conditions if the lease was silent on restoration duties yet authorized the lessee to alter the land. In the end, because of the uncertainty these decisions created, the State enacted a complex regulatory scheme which offers the prospect of some rationality and more uniform standards but still portends uncertainty for landowners and the oil and gas industry given that it has not completely removed courts and judges from the dispute resolution process.

**B. Application of Insurance Proceeds in the Wake of the 2005 Hurricane Season**

My second example of a situation in which a dramatic change of conditions has shed new light on waste conflict arises out of the wreckage of the historic 2004-2005 hurricane seasons which saw Hurricanes Jeanne, Katrina, Rita and Wilma cause catastrophic loss of life and property damage all along the American Gulf Coast. In addition to these terrible losses, the hurricane also spawned an interesting set of mortgage cases implicating the rules governing waste and application of insurance proceeds. These cases illustrate both the importance of contractual language anticipating a sudden change of circumstances and the possibility of waste and the background principles of good faith and fair dealing that inform section 4.7 of the Restatement (Third) of Property: Mortgages.

1. Judicial Enforcement of Application of Proceeds Clauses

One recent decision from New Orleans illustrates what will come as no surprise to many readers — namely, that in the context of a commercial mortgage, courts will enforce express contractual language granting a mortgagee absolute discretion to apply insurance proceeds to reduce an outstanding loan balance, regardless of the mortgagor’s professed desire for or need to use the insurance proceeds for some other purpose, including restoring the damaged property. In this decision, *Strouse Greenberg Properties IV Ltd. Partnership v. CW Capital Asset Management LLC*, the federal district court held that the note holder for a New Orleans multi-family apartment complex which was completely destroyed by Katrina was entitled to a preliminary injunction to prevent the mortgagor from spending $5 million in flood insurance proceeds on rebuilding the complex in another location outside New Orleans.  


204. 442 F. Supp. 2d 313, 321 (E.D. La. 2006). In fact, the property owner hoped to use the insurance proceeds to commence planning for rebuilding and to make a claim for a much larger fund of commercial property insurance to which it might have been entitled. *Id.* at 320.
The court’s rationales are predictable and reasonable. They include not only that the owner was required to provide the flood insurance policy under the mortgage’s general hazard insurance clauses and that the mortgage documents clearly gave the note holder absolute discretion to collect the insurance payments and apply them to the loan balance, but also the court’s more subjective determination that the public interest in enforcing this mortgage contract outweighs any public interest in allowing the owner to use the proceeds for “an unrelated rebuilding effort at another site outside the New Orleans area.”

Would the court have ruled differently if the owner had announced plans to rebuild the apartment complex on site and provide much needed affordable housing for New Orleans’ low income residents? Perhaps that might have affected the court’s ruling at the preliminary injunction hearing, but it would probably not have changed the case’s ultimate outcome given the express contractual language allowing the mortgagee to apply insurance proceeds at its discretion.

In another set of decisions arising from hurricane damage or destruction of single family residences subject to a mortgage, we see a similar outcome but much more anxiety and hesitancy in courts’ thinking about waste and insurance proceeds application. In the most interesting of these decisions, Bean v. Prevatt, a Florida District Court of Appeal held that a private individual lender, who had provided a purchase money mortgage to enable the owner/mortgagor to acquire a lot and mobile home, was entitled to apply insurance proceeds to pay down the outstanding loan balance on the underlying note because the mortgage instrument clearly gave the mortgagee this option. In this case, the mortgagor had borrowed $39,000 and sought to use the proceeds from a windstorm policy to repair his mobile home, which had suffered $12,000 in damages caused by Hurricane Jeanne in 2004. The mortgagee refused to allow this and applied the proceeds to effectively prepay the loan balance until 2016. Interestingly, even though the trial court judge felt bound to enforce the insurance proceed election clause in favor of the mortgagee, he was sympathetic to the “catch 22” plight of the borrower in that the mortgage also apparently contained a standard clause prohibiting the mortgagor from committing waste by allowing it to fall into disrepair. Trying his best to reconcile these two provisions, the trial court judge ruled that if the mortgagee applied the insurance proceeds to the loan balance he would be estopped from foreclosing in the future based on the borrower’s failure to

205. Id. at 320-21.

206. It is noteworthy here that the borrower somehow was able to cash millions of dollars worth of flood insurance checks made out jointly to the note holder and the borrower/owner. Id. at 315. This fact undoubtedly raised a red flag of caution to the court and made it receptive to the note holder’s claim for a preliminary injunction. Counsel for the note holder informed the author in person that the case settled soon after the preliminary injunction ruling.

repair the property and prevent waste.\textsuperscript{208} In effect, the trial court put the mortgagee in a "catch 22" as well. The district court of appeal affirmed, concluding that "as long as the outstanding indebtedness on the agreement exceeds the amount of the insurance settlement, the agreement gives [the mortgagee] the sole and unfettered right to decide whether the insurance payment is used to repair [the borrower's] home," even though it appeared, as the court of appeal noted, that the mortgagee's security interest would have been better protected by repairing the property than by the partial forced pre-payment.\textsuperscript{209}

In another and probably easier case to decide, a federal district court in Florida followed \textit{Bean} in enforcing a mortgagee's option to apply proceeds derived from a forced place insurance policy to pay down a nearly $1,000,000 outstanding loan balance on a residence that was severely damaged by Hurricane Wilma, again relying on the fact that the mortgage clearly gave the lender this option.\textsuperscript{210} Here, however, just as in \textit{Bean}, the court also stated that the mortgagee would be estopped from foreclosing on the property based on an allegation that the borrower failed to repair the property.\textsuperscript{211} The court did not offer any new reasons for its adoption of the estoppel policy created in \textit{Bean}, seemingly content that such an estoppel was a justifiable restraint that could be imposed on the mortgagee for not allowing the mortgagor to use insurance proceeds to rebuild.

\textsuperscript{208} \textit{Id.} at 559.
\textsuperscript{209} \textit{Id.} at 560.
\textsuperscript{211} \textit{Id.} at *2. In \textit{Sussman}, the loan also appears to have involved seller financing, but the origin of the loan is not exactly clear. \textit{Id.} at *1. The decisions in \textit{Bean} and \textit{Sussman} both relied on two earlier Florida decisions that reached similar results with the additional caveat that a mortgagee's contractual right to apply insurance proceeds to outstanding mortgage balance is not diminished by the facts that a mortgagee has already foreclosed on the subject property and the foreclosure sale proceeds are insufficient to cover the full amount of the mortgage debt. Cayer v. Mid-State Fed. Sav. Bank (\textit{In re Cayer}), 150 B.R. 829, 831 (Bankr. M.D. Fla. 1993); Sea Isle Operating Corp. v. Hochberg, 198 So. 2d 336, 337 (Fla. Dist. Ct. App. 1967). As the latter decision points out, the only way that subsequent foreclosure proceedings would extinguish a mortgagee's right to apply the insurance proceeds would be if the debt evidenced by the note and mortgage had been fully discharged. \textit{Sea Isle}, 198 So. 2d at 337. In yet another recent insurance proceed application case that arose out of an accidental fire, a South Carolina court held that a mortgagee was entitled to withhold insurance proceeds paid under the applicable policy and apply them to the loan balance where the mortgage instrument expressly granted the mortgagee this option among three others, even though the lender had already released a portion of the proceeds to the borrower so that she could begin paying a builder and even though the builder was thus required to refinance complete restoration at a much higher interest rate than under the previous mortgage. Brannon v. Palmetto Bank, 638 S.E.2d 105, 107-08 (S.C. Ct. App. 2006).
In a particularly intriguing part of its opinion in Bean, the Florida district court of appeal observed that the outcome in that case fortunately deviated from most lenders' common practice of handling hurricane related insurance proceeds in Florida and commented on the social consequences of that practice:

It should be obvious, however, that the economies of many Florida communities would have been devastated in 2004 if lenders had uniformly followed [the mortgagee's] lead. Fortunately, it appears that most lenders place such money into escrow and merely monitor the funds to assure that they are used to repair the properties that serve as collateral for their loans.212

This observation no doubt reflects the widespread usage of the standard Freddie Mac/Fannie Mae mortgage/deed of instrument for conventional residential mortgage loans which specifically provides that a borrower is entitled to use insurance proceeds to rebuild as long as the proceeds, together with other available funds, make restoration economically feasible and the lender’s security is not impaired.213

Despite the common and beneficent practice it observed in connection with the use of insurance proceeds, the court nevertheless suggested that the Florida Legislature enact regulation to protect homeowners from unscrupulous lien holders. The court even went so far as to enumerate the key provisions of such a scheme. Specifically, it recommended that a lender should be prohibited from applying loan proceeds solely to the mortgagor’s indebtedness, without permitting repair,

if (1) the borrower is not in default at the time of the casualty, (2) there are sufficient funds to complete the necessary repairs in accordance with state and local building regulations, (3) the repairs can be made within a reasonable time (e.g., within a year), and (4) the repaired value of the property will exceed the amount of the remaining principal on the loan.214

Here then is a clarion call, so far apparently unheeded, for public regulation of what would normally be considered a private waste dispute subject to detailed private ordering. What seems to be inspiring the court’s demand for public law intervention is the prospect that self-interested action on behalf of mortgagees could lead to widespread negative spillover effects on an entire community’s ability to recover from a catastrophe. In short, we see once

212. Bean, 935 So. 2d at 560.
213. See Randolph, supra note 76, at 8-9, 15, 20.
214. Bean, 935 So. 2d at 560 n.4.
again the rule-bending pressure for change that dramatically altered circumstances can exert on waste law.

2. Forbearance Practice in the Mortgage Industry in the Wake of Disaster

There are two other important phenomena to note here in relation to how mortgage law and insurance proceeds have intersected in the aftermath of the 2005 hurricane season. In the initial weeks and months after Katrina, many observers and politicians predicted a catastrophic rash of foreclosures on residential mortgage loans along the Gulf Coast that would leave thousands of mortgagors facing bankruptcy and lenders holding billions of dollars of worthless property.\(^{215}\) This initial fear was justified to some degree because immediately after Katrina the percentage of delinquent home mortgage loans on the Gulf Coast did increase dramatically.\(^{216}\) The much feared surge in foreclosures, however, never occurred. In fact, statistics issued by the Mortgage Bankers Association demonstrate that delinquency rates decreased substantially and steadily from their immediate post-Katrina and Rita highs.\(^{217}\)


\(^{216}\) See THE BROOKINGS INSTITUTION METROPOLITAN POLICY PROGRAM AND THE GREATER NEW ORLEANS COMMUNITY DATA CENTER, THE KATRINA INDEX, 55 (Jan. 17, 2007) (hereafter JAN. 2007 KATRINA INDEX), available at http://www.brookings.edu/reports/2007/08neworleansindex.aspx (follow the link to JANUARY 2007 INDEX) (reporting statistics provided by Mortgage Bankers Association through the third quarter of 2006). Right after Katrina and Rita hit the Gulf Coast, the total number of mortgage loans past due surged to 24.6% in Louisiana in the third quarter of 2005 and only fell to 20.8% in the fourth quarter. Id. The numbers in Mississippi were similar but not quite as high: 17.4% and 16.9% in the third and fourth quarters of 2005 respectively. See THE BROOKINGS INSTITUTION METROPOLITAN POLICY PROGRAM AND THE GREATER NEW ORLEANS COMMUNITY DATA CENTER,THE KATRINA INDEX, 45 (Dec. 13, 2006) (hereafter DEC. 2006 KATRINA INDEX) available at same web site as above by following link to DECEMBER 2006 INDEX)

\(^{217}\) See JAN. 2007 KATRINA INDEX, supra note 216, at 55 (showing that overall delinquency rates continued to decline throughout 2006 with the total number of mortgage loans past due declining from 13.7% in the first quarter of 2006 to 9.5% in the third quarter, a percentage that is still higher, however, than the national average of 4.84% for the third quarter of 2006). In the fourth quarter of 2006, total loans in delinquency in Louisiana decreased even further to 9.10%, compared to the 5.31% national percentage. See MORTGAGE BANKER’S ASS’N, NATIONAL DELINQUENCY SURVEY FOURTH QUARTER 2006 (on file with author).
Even more important, foreclosure rates in Louisiana actually fell dramatically so that by the third quarter of 2006 only 1.65% of all loans were in foreclosure (a rate that was actually below the state's foreclosure rate for all of 2004), and 1.86% of all loans were in foreclosure in the fourth quarter of 2006 (a rate roughly equal to the pre-Katrina 2004 rate). The data on Mississippi tells an almost identical story, with foreclosure rates that were actually lower post-Katrina than before the storm for a significant period of time. Even in the sub-prime loan category, the percentage of mortgage loans in foreclosure in Louisiana in the third quarter of 2006 remained roughly consistent with pre-Katrina figures and was only a few percentage points higher than in the United States as a whole. As the graph on the following page demonstrates, this remarkable and surprising resiliency in mortgagor-mortgagee relationships that began right after Katrina has continued well into 2007, with mortgage foreclosure starts and inventories for all loans remaining stable in Louisiana through the second quarter of the year.

In the Greater New Orleans area, which suffered especially catastrophic damage, the number of foreclosure sales for all of 2006 was a remarkably low 307 – roughly a third of the lowest annual number of foreclosure sales over the last 20 years. A recently published study of mortgage foreclosure in post-Katrina New Orleans based on an examination of writs leading to foreclosure filed in the Orleans Parish Recorder of Mortgages confirms the general trends I have reported above. Despite higher rates of residential mortgage defaults in the affected area, there was, in fact, a reduction in the rate of foreclosure activity in the year following Katrina in Orleans Parish.

218. JANUARY 2007 KATRINA INDEX, supra note 216, at 55. In 2004, the foreclosure rate in Louisiana hovered between 1.8% and 1.7%. In 2005 prior to Katrina, it had dropped slightly further to 1.6% and 1.4% in the first and second quarters respectively. Id. The fourth quarter data is found in Mortgage Bankers Ass'n, National Delinquency Report and in THE BROOKINGS INSTITUTION METROPOLITAN POLICY PROGRAM AND THE GREATER NEW ORLEANS COMMUNITY DATA CENTER, THE KATRINA INDEX, 17-18 (June 2007) available at same web site referenced in note 217 by following link to JUNE 2007 INDEX).

219. See DEC. 2006 KATRINA INDEX, supra note 216, at 45. According to the NATIONAL DELINQUENCY SURVEY, supra note 217, in the fourth quarter of 2006, Mississippi’s percentage of all loans in foreclosure climbed to 2.16%, a rate that was still just equal to that at the end of 2004 and the beginning of 2005.

220. JAN. 2007 KATRINA INDEX, supra note 216, at 53 (revealing a 5.54% foreclosure rate for sub-prime loans in Louisiana, compared to a 3.86% rate nationwide and rates that hovered between 5.3% and 6.5% in 2004 in Louisiana). In the fourth quarter, the percentage of sub-prime loans in foreclosure increased to 6.55%, a figure equal to first quarter 2004 numbers and by no means the highest in the nation. See id.; NATIONAL DELINQUENCY SURVEY, supra note 217.

221. Statistics compiled by the RESEARCH DIVISION OF LATTER AND BLUM, INC. REALTORS, NEW ORLEANS, LOUISIANA (on file with author).

What accounts for this relative stability and resiliency or at least absence of foreclosures? For one, the remarkable risk-spreading structure of the secondary mortgage market\(^{223}\) allowed major mortgage holders to forbear on mortgage payment obligations for many months (in some cases for up to a year) while homeowners put their lives back in order, returned to work, made insurance claims and fought with insurance companies to obtain adequate

\(^{223}\) For an overview of the development of the secondary mortgage market, see Nelson & Whitman, supra note 55, § 11.3; Robin Paul Malloy, The Secondary Mortgage Market: A Catalyst for Change in Real Estate Transactions, 39 S.W. L.J. 991, 998 (1986).
insurance settlements. In addition, the presence of the standard Freddie Mac/Fannie Mae insurance proceed application clause in thousands of mortgage documents, backstopped by the advocacy of a rule of reasonableness and the endorsement of an implied covenant of good faith and fair dealing in section 4.7(c) of the Restatement (Third) of Property: Mortgages, also helped create a mortgagee-mortgagor culture of mutual accommodation that enabled many thousands of homeowner mortgagors to get back on their feet and, as the court in Bean v. Prevatt noted, eventually begin using their insurance proceeds to rebuild their homes and lives. No doubt some mortgagor/homeowners were pressured into or felt constrained by their own uncertain economic prospects and lack of additional financial resources to apply their insurance proceeds to pay down or pay off their mortgage balances. But so far allegations of widespread lender abuse in this area have not materialized.

3. Miscellaneous Proceeds and the Road Home

Finally, the basic background principles of mutual accommodation between mortgagor and mortgagee that are outlined in section 4.7(c) of the Restatement (Third) of Property: Mortgages have also recently become crucial as Louisiana struggles to disburse the roughly $7.5 billion worth of Federal Community Development Block Grant funds that it has dedicated for compensating Louisiana homeowners whose homes were destroyed or damaged.

224. Immediately after the storms’ destruction, for instance, Freddie Mac implemented a blanket moratorium on foreclosures in all Louisiana parishes affected by Hurricanes Katrina and Rita lasting until August 31, 2006 and further allowed almost 18,000 borrowers to delay the resumption of their mortgage payments. As a result of these policies, less than one percent of Freddie Mac’s borrowers had been subject to foreclosure as of January 2007. Mary Judice, La. Sees Surge in Mortgage Defaults, NEW ORLEANS TIMES PICAYUNE, Jan. 14, 2007, available at 2007 WLNR 762145. Fannie Mae, another even bigger buyer and bundler of mortgages in the secondary market, also implemented a foreclosure moratorium and provided 35,000 borrowers extra time to make payments after the storms. Id.; Mary Judice, Lenders Try Not to Foreclose in N.O., NEW ORLEANS TIMES PICAYUNE, Feb.21, 2006, available at 2006 WLNR 2988888. For a general report on the mortgage industry’s forbearance practices after Katrina, see Fin. Servs. Roundtable, Accelerating the Katrina Recovery: An Interim Report by the Blue Ribbon Commission on Mega-Catastrophes of the Financial Services Roundtable 27-28 (Oct. 25, 2006), available at http://www.fsround.org/publications/pdfs/KATRINAFinalDocument.pdf. See also John Dalton, President, Financial Services Roundtable Housing Policy Council, Testimony of the Housing Policy Council of the Financial Services Roundtable to the House Financial Services Committee 3, 5-6 (Feb. 6, 2007), available at http://www.fsround.org/media/testimony.htm (follow the “Testimony on Katrina February 6, 2007” hyperlink).
by Hurricanes Katrina and Rita and that were uninsured or underinsured. As a result of a recent change of policy mandated by the U.S. Department of Housing and Urban Development, Louisiana's initial plan to disburse its "Road Home" rebuilding grants through carefully monitored escrow accounts has been scrapped and now Louisiana is distributing its rebuilding grants of up to $150,000 by simply writing checks to eligible homeowners. When those checks are paid to homeowners-mortgagors whose homes are subject to mortgages, the checks will likely be considered "miscellaneous proceeds" under yet another provision in the standard form Freddie Mac/Fannie Mae uniform mortgage instrument. Fortunately, that instrument establishes a base line norm that these proceeds, just like insurance proceeds, be used for restoration or repair of the property as long as restoration is economically feasible and the lender's security is not lessened. In this case, the livelihoods of many thousands of Louisiana homeowners will depend on whether mortgagees continue to act, as Professors Stoebuck and Whitman suggest through their work on the Restatement (Third) of Property: Mortgages, with the goals of cooperation and preservation of the long-term interests of both mortgagor and mortgagee in mind.

IV. CONCLUSION

Transformations in waste doctrine, as distilled in key Restatement of Property provisions and in classic treatises, and as revealed in the two contemporary outbreaks of waste conflict discussed above, are indeed significant windows into American property law. What has become clear, I hope, through this examination of waste doctrine is the important role that the concepts of reasonableness, good faith and fair dealing can play in solving waste conflicts. The deep current that ties these waste discussions and conflicts together is not so much disagreements about how to determine whether the market value of a future interest holder's inheritance has been diminished or how to measure the impairment of a mortgagee's security interest or exactly how much it will cost to clean up contamination on a South Louisiana oilfield site or back fill a pipeline canal. Instead the underlying current is a more fundamental dispute about how and whether we should impose external stan-

225. For detailed discussions of how Louisiana's "Road Home" homeowner assistance program emerged and how it is being implemented, see John A. Lovett, Rebuilding a Region, Housing Recovery Efforts in the Wake of Katrina and Rita, PROB. & PROP., Sept./Oct. 2006, at 49, 52-53; and Lovett, supra note 17.


227. See Fannie Mae/Freddie Mac Uniform Mortgage, supra note 65, app. & 11, at 1211.

228. Id.
standards for the behavior of parties who are locked into long term property relationships in which both parties' interests are not always aligned.²²⁹

What these waste conflicts teach us is that courts, legislators, law reformers and scholars like Dale Whitman have continually felt compelled to create waste standards that either explicitly or implicitly hold both parties to some external standards of reasonableness—fuzzy as they sometimes may be—that are grounded in principles of fairness, respect for the other parties' legitimate needs, long-term relationship preservation and concern for ameliorating the external spillover effects of the parties' behavior on the larger community. Whether this tendency is in the long run healthy for property law is a subject beyond the scope of this article, but it is one that we should continue to evaluate by refocusing our attention on episodes of radical change in waste doctrine.

²²⁹. See generally Freyermuth, supra note 73.